

**REPORT OF THE COMMITTEE
TO EXAMINE THE LEGAL AND OTHER DIFFICULTIES
FACED BY BANKS AND FINANCIAL INSTITUTIONS
IN REHABILITATION OF SICK INDUSTRIAL UNDERTAKINGS
AND SUGGEST
REMEDIAL MEASURES INCLUDING CHANGES IN THE LAW**



**RESERVE BANK OF INDIA
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LIST OF ABBREVIATIONS

RBI	— Reserve Bank of India
IDBI	— Industrial Development Bank of India
LIC	— Life Insurance Corporation of India
IRCI	— Industrial Reconstruction Corporation of India Ltd.
IFCI	— Industrial Finance Corporation of India
ICICI	— Industrial Credit and Investment Corporation of India Ltd.
GIC	— General Insurance Corporation of India
UTI	— Unit Trust of India
I (D & R) Act	— Industries (Development & Regulation) Act, 1951.
MRTP Act	— Monopolies and Restrictive Trade Practices Act, 1969.
SFC	— State Financial Corporation
SIUD	— Sick Industrial Units Division
IBA	— Indian Banks' Association
BIR	— Board for Industrial Revival
IECD	— Industrial & Export Credit Department
SCC	— Standing Co-ordination Committee
CAS	— Credit Authorisation Scheme
DESACS	— Department of Statistical Analysis and Computer Services
BSR	— Basic Statistical Returns
ASSOCHAM	— Associated Chambers of Commerce and Industry of India
NEB	— National Enterprise Board

CHAPTER I

INTRODUCTION

Industrial sickness tends to cause loss of production very often leading to unemployment/loss of employment and resulting in blocking of scarce resources of the banks and financial institutions, besides entailing loss of substantial revenue to the exchequer. The magnitude and incidence of industrial sickness are matters of serious concern for the Central and State Governments, Reserve Bank of India, banks and financial institutions, not merely due to the above factors, but also because such a trend undermines public confidence in the functioning of the organised sector with attendant repercussions on the overall investment climate in the economy of the country.

1.2 While the general problem of industrial sickness has been engaging the attention of all concerned, efforts were afoot by the Central Government in consultation with the RBI to sort out the problems of rehabilitation of sick industrial units. Thus, the Central Government, Government of West Bengal, RBI, Industrial Development Bank of India, Life Insurance Corporation of India and banks at a joint meeting held in July 1970 at Calcutta took certain basic decisions regarding rehabilitation of sick industrial units. Pursuant thereto the Central Government decided upon institutionalisation of rehabilitation efforts and at their initiative the RBI and IDBI contemplated the formation of a central agency initially to take care of the rehabilitation of sick industrial units in the Eastern Region. Accordingly, the Industrial Reconstruction Corporation of India Ltd. was set up in April 1971 with its headquarters at Calcutta mainly to fortify the institutional structure for the provision of reconstruction and rehabilitation assistance to sick and closed industrial units.

1.3 Since the formation of the IRCI, the RBI has been taking several measures for bringing about effective co-ordination amongst the banks and financial institutions in their efforts in rehabilitating sick industrial units. In this context, the RBI convened a meeting of the banks, IDBI and IRCI at Calcutta in December 1974 where the various problems encountered in rehabilitating sick industrial units by the participants were mutually discussed.

1.4 Even during 1975 the Study Group appointed by the RBI to frame guidelines for follow up of bank credit (popularly known as Tandon Committee) in its report recognised the need for the banks to include in the rehabilitation proposals of sick industrial units, financial/structural re-organisation as also intervention by the banks in the management of sick industrial units.

1.5 The financial institutions were also engaged simultaneously in providing to sick industrial units, reliefs such as additional financial assistance, adjustment in respect of interest rate/payment of interest, rescheduling of existing loans and conversion of short-term liabilities into long-term obligations. Due attention was also paid to aspects like management deficiencies and imbalances in technical and production levels as part of the rehabilitation packages. Such rehabilitation packages are formulated by the lead financial institution in mutual consultation with the participating institutions/banks and other agencies. Rehabilitation efforts have assumed a significant place in the post-sanction supervision functions of the financial institutions. In order to achieve effective monitoring and nursing of sick industrial units, the financial institutions have set up separate rehabilitation cells in their respective organisations manned by suitable personnel with suitable technical/financial and managerial capabilities.

1.6 In spite of the co-ordinated approach thus set in motion as set out above, it was observed that there was no significant impact on the incidence of sickness amongst the industrial units. In order to rationalise the procedures obtaining in the banks in regard to sick industrial units, the RBI drew up a scheme in May 1976 according to which the banks were urged to strengthen their internal organisation such as building up of capability for analysing and interpreting the data obtained under the information system, speedy communication between the operating levels and the head offices regarding the units which show signs of sickness, etc. Simultaneously, the RBI also established a cell, since strengthened into the Sick Industrial Units Division to function as a clearing house for information relating to sick industrial units and act as a co-ordinating agency amongst the Central and State Governments, banks, financial institutions and other agencies for tackling various related issues. Banks were advised that the cells dealing with the problems of industrial sickness in their offices should function in close co-ordination with the RBI.

1.7 While steps as set out above were being taken by the RBI, the Government of India had constituted in May 1976 a high level working group headed by Shri H. N. Ray, Secretary, Ministry of Finance, Government of India, to go into the question of the feasibility of merging productive enterprises which were in financial difficulties or were ailing, with sound units so that the combined unit would function more effectively. In its report dated 31st July 1976, the Committee while making recommendations governing mergers, recommended, inter alia, that in order to avoid a heavy drain on the exchequer it is necessary to explore ways in which potentially viable sick industrial units can be revived

through voluntary merger with sound units and suggested that a special scheme may be implemented through an enabling legislation to supplement the existing legal provisions regarding merger and reconstruction under the Companies Act, 1956.

1.8 In November 1976, the RBI advised the banks to set up cells at their important regional centres as well, besides the cells at their head offices and provide expert staff including technical personnel, for rehabilitation of sick industrial units. It was further enjoined on the banks by the RBI that the former should analyse the various causes of sickness and assess the various concessions, etc. to be given to the sick industrial units. The banks were asked specifically to plan a time frame of say, about 2 months, within which the financing banks should come up with the necessary proposals for assistance to the sick industrial units, once the commercial viability of the latter was established. Where the banks themselves might not be in a position to provide the assistance required, e.g., long term loans, interest free or low interest funds, concessions in the matter of taxation, adequate and regular supply of inputs including power, change in the management of the sick industrial unit, etc. they were advised by the RBI in December 1978 to refer such cases to the IDBI to consider the package of measures necessary for rehabilitation.

1.9 Similarly in respect of sick small scale industrial units, the RBI in May 1978 drew the attention of the banks to revamp the organisational arrangements at their regional offices and at centres where **Small scale industrial units** financing of small scale industrial units was concentrated and to set up regional cells to render the necessary monitoring and counselling assistance. Where sickness was due to lack of power, raw materials etc. the banks were advised to refer such cases to the State Level Co-ordination Committees which had representatives from the banks and financial institutions, State Governments, Small Industries Service Institutes, etc. In 1980 the State Level Inter-Institutional Committees were set up to discharge functions identical to those of the State Level Co-ordination Committees. After their reconstitution in 1981 these committees are at present functioning under the convenorship of the RBI with the Secretaries, Industries Departments of the respective State Governments as their chairmen. These committees, besides providing a useful forum for exchange of information and discussion on the problems faced by small and medium scale industrial units and small entrepreneurs, also deal with the problems relating to :

- i) co-ordination between the banks and financial institutions;
- ii) provision of adequate infrastructural facilities to industrial units; and

iii) general problems relating to such units.

1.10 The Government of India in November 1981, inter alia, decided that the banks should refer to the IRCI cases of sick industrial units which have not been granted financial assistance by the term lending institutions for formulating rehabilitation packages and other assistance required by them. Accordingly, the banks were advised by the RBI to continue to refer the cases of sick industrial units to the IDBI where term lending institutions were already involved in financing.

1.11 In January 1981, the RBI convened a meeting of the chairman, IDBI, chief executives of other term lending institutions, viz. IRCI, Industrial Finance Corporation of India, Industrial Credit and Investment Corporation of India Ltd., LIC, General Insurance Corporation of India and chairmen of commercial banks. Senior government officials also participated in the discussions. The meeting was presided over by the then Deputy Finance Minister, Government of India. Deliberations in the meeting covered various important issues for effectively tackling the problems of industrial sickness, viz. those relating to taxation measures, changes required in the legislative provisions of various statutes such as the Companies Act, 1956 and the Industries (Development & Regulation) Act, 1951, etc. and also the toning up of internal systems of the banks and financial institutions to ensure that incipient sickness was detected at an early stage and tackled effectively by co-ordinated action between the banks and financial institutions.

1.12 In accordance with one of the decisions taken at the aforesaid meeting, the RBI vide its Memorandum dated 14th May 1981, appointed a Committee consisting of the following members to examine the legal and other difficulties faced by the banks and financial institutions in rehabilitation of sick industrial undertakings and suggest remedial measures, including the changes required in various laws, under the Chairmanship of Shri T. Tiwari, Chairman, IRCI, Calcutta.

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|---------------------------|----------|
| 1. Shri T. Tiwari | Chairman |
| Chairman | |
| Industrial Reconstruction | |
| Corporation of India Ltd. | |
| Calcutta | |
| 2. Dr. P. D. Ojha | Member |
| Executive Director | |
| Reserve Bank of India | |
| Bombay | |

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| 3. Shri R. Viswanathan
Chief General Manager
State Bank of India
International Division
Central Office
Bombay | Member |
| 4. Shri R. Sreekrishnan*
Chief Officer (Law)
State Bank of India
Bombay | Member |
| 5. Shri Y. V. Sivaramakrishnayya
Chairman & Managing Director
Bank of Baroda
Bombay | Member |
| 6. Shri K. L. Roy
Chairman
United Bank of India
Calcutta | Member |
| 7. Shri S. A. Naik
Legal Adviser
Industrial Development
Bank of India
Bombay | Member |
| 8. Shri R. Jagannathan
General Manager
Industrial Development
Bank of India
Madras | Member |
| 9. Shri D. N. Davar
Executive Director
Industrial Finance
Corporation of India
New Delhi | Member |
| 10. Shri C. Chandrasekhar
Deputy General Manager
(Operations)
Industrial Credit & Investment
Corporation of India Ltd.
Bombay | Member |

* Shri M. K. Chubby Raj, Law Officer, State Bank of India, replaced Shri R. Sreekrishnan with effect from 10th April 1982.

11. Shri M. N. Govindaraj*
 Deputy Chief Officer
 Industrial Credit Department
 Reserve Bank of India
 Bombay

Member-Secretary

The terms of reference of the Committee are as follows :

- (i) To review the present policy framework (including legal provisions) within which banks/financial institutions can bring about a change in the management of industrial units assisted by them and to make recommendations as to the changes considered desirable with a view to ensuring that the industrial units operate viably.
- (ii) To review the existing criteria adopted by banks/financial institutions in determining the suitability of a sick unit for revival and to recommend appropriate modifications therein, keeping particularly in view the need to have a reasonable time-frame for any programme of revival.
- (iii) To identify the main constraints in the matter of rehabilitation of sick units, the problems faced by the banks/financial institutions involved and to suggest remedial measures including amendments to the various statutes.
- (iv) To suggest measures including amendments to legal provisions which would facilitate the restructuring of the capital base of the assisted units.
- (v) To identify in a general way, what are the concessions which should normally be made by the various agencies involved in the revival, including management and workers, and in that context, whether sick units should be burdened with obligations like payment of minimum bonus and implementation of various wage awards, etc. which may be having adverse effects on the rehabilitation programmes.
- (vi) To suggest stand-by institutional arrangements (other than nationalisation) for purchase of undertakings or shares in companies owning the undertakings, in the absence of private purchasers or in competition with them, in the case of viable units so as to protect to the maximum extent possible, the institutional funds already involved in the undertakings.

* Shri S. Jayaraman, Joint Chief Officer, Industrial Credit Department, RBI, Bombay, took over as Member-Secretary with effect from 12th August 1982 in place of Shri M. N. Govindaraj vide the RBI's Memorandum dated 7th August 1982.

- (vii) To identify the factors inhibiting expeditious mergers of sick units with the healthy ones and to suggest remedial measures for expediting such mergers.
- (viii) In cases where it is deemed necessary to dispose of certain/all the assets of the units — to suggest legal measures including amendments to the Land Ceiling Acts, etc., so as to expedite the legal process for speedy realisation of the dues of the banks/financial institutions.
- (ix) To review broadly the difficulties faced by the banks and financial institutions in the case of units taken over by Government under I (D & R) Act, 1951 and to suggest remedial measures.

and

- (x) To make such other suggestions and recommendations which in the opinion of the Committee are expedient for speeding up revival of the sick units.

1.13 At its first meeting on 19th June 1981, the Committee felt the need for associating an economist of independent status as a member of the Committee. In view of his long and varied experience in the field, Dr. R. K. Hazari (Ex-Deputy Governor, RBI) was appointed by the RBI as a member of the Committee vide Memorandum dated 12th October 1981.

1.14 At its first meeting, the Committee, while examining the available legal framework for the rehabilitation of sick industrial units, observed that no specific law as such was dealing with the problem of rehabilitation of sick industrial units. There were legal hurdles in reconstruction/rehabilitation of sick industrial units. Even the IFCI Act and the State Financial Corporations Act dealt with the modes of recovery and not those of rehabilitation. In this context, it was felt that the framing of a suitable special legislation designed to enable the speedy and effective implementation of rehabilitation programmes of sick industrial units was called for.

1.15 Pursuant thereto a Legal Sub-Committee under the Chairmanship of Shri S. A. Naik*, Legal Adviser, IDBI was constituted by the Committee at that meeting with the following members to study the existing provisions in various legislations so as to review (i) whether there are inconsistencies in them and (ii) how far such legal provisions act as hurdles in the speedy implementation of rehabilitation programmes of sick industrial undertakings.

* Also member of the Committee.

1. Shri A. K. Ghose
Legal Adviser
Industrial Finance Corporation of India
New Delhi
2. Shri C. Chandrasekhar*
Deputy General Manager (Operations)
Industrial Credit and Investment
Corporation of India Ltd.
Bombay
3. Shri R. Krishnan
Joint Legal Adviser
Reserve Bank of India
Bombay
4. Sri Sai P. Ram Chandra Rao
Deputy General Manager (Law)
Industrial Reconstruction
Corporation of India Ltd.
Calcutta
5. Shri R. Sreekrishnan*
Chief Officer (Law)
State Bank of India
Bombay

1.16 In the context of the study referred to above and also with reference to the objectives of the Committee, the Legal Sub-Committee was requested to consider preparing necessary amendments to the provisions of various existing legislations or in the alternative, frame a comprehensive legislation in such a manner as to enable the banks and financial institutions to implement the task of rehabilitating the sick industrial units successfully without any legal impediments. To consider the enactment of a special legislation for ensuring timely action for recovery of dues/revival of sick industrial units and revival of or even enlargement of the recommendations of the H. N. Ray Committee referred to in paragraph 1.7 above, the Secretary, Ministry of Finance, Department of Economic Affairs (Banking Division), Government of India, convened a meeting on 18th July 1981. At that meeting there was a general recognition that the present statutory provisions of the Companies Act, 1956, Monopolies and Restrictive Trade Practices Act, 1969 and the procedures prescribed thereunder proved to be serious impediments in expeditious finalisation of schemes of rehabilitation/merger of sick industrial undertakings. The Secretary,

* Also members of the Committee

Ministry of Industry, had even made a suggestion that the banks and financial institutions themselves should be vested with statutory powers of a non-justiciable nature to deal with such cases. It was, therefore, decided to strengthen the Committee with additional members from the Government as also to enlarge its terms of reference. Accordingly the following members were included in the Committee vide RBI's Memorandum dated 16th September 1981 :

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| 1. Shri D. R. Mehta
Joint Secretary
Banking Division
Department of Economic Affairs
Government of India
New Delhi | Member |
| 2. Shri S. C. Mittal
Joint Secretary
Department of Company Affairs
Government of India
New Delhi | Member |
| 3. Shri P. K. Ahuja
Director
Department of Industrial Development
Government of India
New Delhi | Member |
| 4. Dr. V. K. Agarwal*
Deputy Legal Adviser
Department of Legal Affairs
Government of India
New Delhi | Member |

1.17 These members were also included in the Legal Sub-Committee. It was further decided that the above Sub-Committee should consider the different aspects of the proposals for a special legislation for the creation of a special authority and procedures and this Committee should submit an interim report on the subject as early as possible.

1.18 The terms of reference as enlarged vide RBI's Memorandum dated Additional 16th September 1981 are as under :

terms of reference i) To consider the need for any special legislation, its contents and legal feasibility;

* Consequent on Dr. V. K. Agarwal proceeding abroad, the Government of India vide their communication dated 1st February 1982 had deputed Kum. S. V. Maruthi, Deputy Legal Adviser, Department of Legal Affairs, in his place.

- ii) To study the necessity and feasibility of promoting amendments to various laws (in their application to sick units) independently or consequential or supplemental to the special legislation;

and

- iii) To consider the feasibility of recovery of the dues of the financial institutions and banks by adopting the summary procedure obtaining under the Public Demands Recovery Act or similar local laws.

A copy of each of the Memoranda referred to is given in Appendix I. The Committee had 13 meetings at different centres, of which 4 were held in Bombay, 4 in Calcutta, 3 in Delhi and one each in Madras and Bangalore.

1.19 The Legal Sub-Committee had five meetings. Shri T. Tiwari, Chairman, Dr. P. D. Ojha, Member and Shri M. N. Govindaraj, the then Member-Secretary of the Committee attended these meetings and participated in the deliberations. The Legal Sub-Committee submitted its report dated 19th October 1981 on the issue of special legislation. The Committee, in its meeting on 3rd November 1981 held at Calcutta, considered and approved the Report of the Legal Sub-Committee and forwarded its Interim Report to the RBI on 20th November 1981. A copy of the Interim Report is furnished at Appendix II.

1.20 To consider the feasibility of recovery of dues of the banks and financial institutions by adopting the summary procedure obtaining under Sub-Committee on the Public Demands Recovery Act or similar local laws as per item (viii) and item (iii) of the terms of reference Recovery of the Committee, vide Memoranda dated 14th May Dues 1981 and 16th September 1981 respectively, the Committee after much deliberations on this issue appointed a Sub-Committee with Shri D. R. Mehta as Chairman and S/Shri D. N. Davar, R. Krishnan, R. Viswanathan, C. Chandrasekhar, Sri Sai P. Ram Chandra Rao, M. K. Chubby Raj and Kum. S. V. Maruthi as members to examine extensively the need for a special legislation for recovery of dues of the banks and financial institutions and make suitable recommendations. The aforesaid Sub-Committee after deliberating on the various issues during its four meetings, submitted its report to the Committee on 9th June 1983. Recommendations of the Sub-Committee are discussed in Chapter VIII.

1.21 The Committee was required, inter alia, to suggest a workable formula for fixing the reserve price at which a unit could be sold. For **Sub-Committee on Reserve Price** examining this issue, the Committee formed a Sub-Committee with Shri Y. V. Sivaramakrishnayya as Chairman and S/Shri D. N. Davar, C. Chandrasekhar, R. Viswanathan and R. Jagannathan as members. The Sub-Committee submitted its report to the Committee on 11th July 1983. Their recommendations are discussed in Chapter X.

1.22 In examining the terms of reference number (v) of Memorandum dated 14th May 1981, viz. "To identify in a general way, what are **Discussion with representative bodies** the concessions which should normally be made by the various agencies involved in the revival, including management and workers, and in that context, whether sick industrial units should be burdened with obligations like payment of minimum bonus and implementation of various wage awards, etc. which may be having adverse effects on the rehabilitation programme", the Committee felt that it would be desirable to note the views of the concerned groups/bodies before making its recommendations. Accordingly, the Committee had the benefit of discussions/views of the following Chambers of Commerce :

1. The Associated Chambers of Commerce & Industry of India, New Delhi (ASSOCHAM);
2. All India Manufacturers' Organisation, Bombay (AIMO);
3. Indian Merchants' Chamber, Bombay (IMC);
4. Federation of Indian Chambers of Commerce & Industry, New Delhi (FICCI).

The Committee also had the benefit of discussions with/views of the following Central Workers' Organisations from out of the list provided by the Ministry of Labour, Government of India :

1. All India Trade Union Congress, New Delhi (AITUC);
2. The Hind Mazdoor Sabha, Bombay (HMS);
3. The Bharatiya Mazdoor Sangh, New Delhi (BMS);
4. The Centre of Indian Trade Unions, New Delhi (CITU);
5. Indian National Trade Union Congress, New Delhi (INTUC).

The Committee also had discussions with the chairmen of all-India term lending institutions who were members of the Inter-Institutional Meeting and also the chairmen and the members of the managing committee of the Indian Banks' Association to elicit their views on its various terms of reference. A copy of each of the notes containing details of certain broad issues relating to the terms of reference on which views were called for from the various organisations, etc., is

given in Appendix III. The response from all the organisations/institutions was good and has assisted the Committee to a very great extent in finalising its views.

1.23 The term 'sick unit' referred to in the terms of reference and the term 'sick industrial unit' appearing in this Report should be construed as being covered by the definition of the 'sick industrial undertaking' as given in the Special Legislation referred to in Chapter IV.

1.24 Chapter II reviews the magnitude and analyses the incidence and causes of industrial sickness.

Chapter III presents a summary of the views/discussions that the Committee had with the various representative bodies of trade, industry, labour, banks and term lending institutions, etc. necessitated by terms of reference number (v) of the Memorandum dated 14th May 1981.

Schema of the Report

Chapter IV contains a review of the existing criteria of viability and packages of rehabilitation of sick industrial units as required by the terms of reference numbers (ii), (iii) and (v) of the Memorandum dated 14th May 1981.

Chapter V presents exercises on Model Case Studies for various alternative packages of rehabilitation having a bearing on the terms of reference number (ii) of the Committee's Memorandum dated 14th May 1981.

Chapter VI covers the Committee's recommendations relating to the enactment of a special legislation for the revival of sick industrial units as dealt with in the Interim Report and covering the terms of reference numbers (i), (iii), (iv), (vii) and (ix) of the Memorandum dated 14th May 1981 and numbers (i) and (ii) of the Memorandum dated 16th September 1981.

Chapter VII deals with the creation of the Board for Industrial Revival as recommended in the Interim Report.

Chapter VIII relates to the terms of reference number (viii) of the Memorandum dated 14th May 1981 and number (iii) of the Memorandum dated 16th September 1981 dealing with recovery of dues of the banks and financial institutions.

Chapter IX covers the term of reference number (v) of the Memorandum dated 14th May 1981, on recommendations relating to the concessions to be made by the various agencies concerned in the rehabilitation of sick industrial units.

Chapter X details the other recommendations of the Committee having a bearing on the terms of reference numbers (vi) and (x) of the Memorandum dated 14th May 1981.

Chapter XI contains a summary of the main recommendations of the Committee.

1.25 The Committee is extremely grateful to the various organisations of trade, industry and labour, the IBA and the all-India financial institutions (as given in Annexure I), who presented their valuable views on the terms of reference during their meetings with the Committee. The keen interest evinced by these organisations is also borne out by the large number of detailed memoranda/notes on the various issues submitted by them to the Committee, which were, no doubt, extremely useful. The Committee was very much benefited by useful discussions with officials of SFCs on certain significant issues with regard to recovery of dues of the banks and financial institutions. Valuable notes/information on various facets of industrial sickness and related issues were made available to the Committee by a large number of institutions and individuals. Amongst the individuals, the Committee is happy to put on record the contribution of Shri Y. H. Malegam, in the form of two notes, one on 'Modernisation vis-a-vis Income-Tax Provisions' and the other on 'Methodology for determining Reserve Price', — both these notes as given in Appendix IV were of extreme use for arriving at decisions by the Committee on the concerned issues. It is no exaggeration to record that Shri W. S. Tambe, the then Executive Director, RBI, during the Committee's first meeting, provided his considered views on the terms of reference of the Committee; these views served as the main guidelines for our further work. We are thankful to S/Shri S. A. Naik, D. R. Mehta and Y. V. Sivaramakrishnayya for heading the three Sub-Committees (referred to in paragraphs 1.14, 1.20 and 1.21 respectively), set up for certain specific matters in addition to their responsibility as members of the Committee. Though Shri R. Sreekrishnan and Dr. V. K. Agarwal could not continue for other pressing reasons, they made valuable contributions during their tenure as members of the Committee. We are also grateful to Shri S. Mukherji, Deputy General Manager, IRCL, for his valuable note on the issue of creation of Industrial Management Pool. We are also thankful to S/Shri A. K. Ghose, R. Krishnan and Sri Sai P. Ram Chandra Rao for valuable contributions as members of the Legal Sub-Committee. We would like to express our deep gratitude and sincere thanks to Shri C. Chandrashekar, for the guidance provided and contribution made while going through the drafts. We would further like to record our warm appreciation of the courtesy and hospitality extended by the various institutions during the Committee's meetings at their respective centres;

special mention in this context may be made of the IRCI. We are thankful to Shri M. N. Govindaraj, Ex-Member-Secretary; for his assistance and also place on record our high appreciation of the untiring and painstaking efforts put in by Shri S. Jayaraman, our Member-Secretary, for his hard, enthusiastic and dedicated work. We are grateful to the Industrial and Export Credit Department, RBI, for providing the Secretariat, particularly to S/Shri R. Bhalla, Industrial Credit Officer, K. Gangadharan and S. Venkatesan, Staff Officers, who assisted the Committee most admirably and in particular to Shri Kripa Shankar, Director for his studies on the magnitude and causes of industrial sickness and the exercises on the Model Case Studies on alternative packages of rehabilitation.



CHAPTER II

MAGNITUDE, INCIDENCE AND CAUSES OF INDUSTRIAL SICKNESS

The main objective of the Committee is to examine the legal and other difficulties faced by the banks and financial institutions in rehabilitation of sick industrial units and suggest remedial measures including changes in the law as may be observed from the terms of reference. It is, therefore, necessary for the Committee to assess first the magnitude and analyse the incidence and causes of industrial sickness. It has to be mentioned in this connection that the Committee did not undertake any field study for the purpose, but largely depended on the various data at present being obtained by the RBI from the scheduled commercial banks and by the IDBI.

2.2 As a follow-up of the decisions taken at the seminar convened by the RBI in 1976, the SIUD of the RBI, in order to have a broad idea of the magnitude and causes of industrial sickness in different industries and the task involved in rehabilitation of sick industrial units, have been obtaining periodical information on sick* industrial units from the scheduled commercial banks financed by them. Detailed data such as the name of the sick industrial unit, nature of its industry, location, causes of its sickness, total amount sanctioned and outstanding from the banking system as a whole and individually from each bank, etc., are thus made available to the RBI by the scheduled commercial banks in respect of sick units, each with a total credit limit of Rs. 1 crore and above from the banking system; in respect of other type of sick industrial units aggregate data are made available. Sick industrial units for which data is supplied by the scheduled commercial banks are classified under major industry groups into (1) Cement (2) Chemicals (3) Engineering and Electricals (4) Iron and Steel (5) Jute (6) Rubber (7) Sugar (8) Textiles and (9) Miscellaneous.

2.3 The IECD of the RBI, for the purpose of operation and monitoring of the Credit Authorisation Scheme is also collecting data from the scheduled commercial banks in respect of all industrial units (whether sick or not), each of which enjoys a total credit limit of Rs. 1 crore and above from the banking

* For this purpose, a unit is to be considered as 'sick' by the bank if the unit has incurred cash loss for one year and in the judgement of the bank, is likely to continue to incur cash losses for the current year as well as the following year and which has an imbalance in its financial structure such as current ratio of less than 1:1 and worsening debt-equity ratio (total outside liabilities to net worth) as per the definition of a sick unit accepted by the Standing Coordination Committee of the RBI.

system. These data are being collected from the scheduled commercial banks since November 1976 in prescribed proformae as at the end of each calendar month and also as at the end of each calendar quarter.

2.4 A third type of statistics, being collected every calendar month by the Department of Statistical Analysis and Computer Services, RBI, from the scheduled commercial banks, is that made **BSR data** available through the Basic Statistical Returns. These data which are mainly collected for the purpose of a sound and objective system of credit planning and its monitoring by the RBI also cover various aspects of credit such as amount sanctioned, disbursed and outstanding amounts of credit by the scheduled commercial banks to various sectors of the economy such as industry, trade, agriculture and within each of these by their respective sub-sectors with further state-wise details.

The Committee made extensive use of the aforesaid three types of data from the RBI for the purpose of assessing the magnitude, incidence and causes of industrial sickness. The other source materials used wherever necessary for the purpose are referred to at appropriate places.

2.5 According to the latest data available with the RBI as supplied by the scheduled commercial banks, as on 31st December 1981, Rs. 2,025 crores was the outstanding bank credit in 26,758 sick units of all types. The outstanding bank credit in the sick industrial units as also the number of such units **Magnituda of industrial sickness :** has also recorded an increase since 1979; the year from **all-India** which such data are uniformly available. It is further observed that substantial proportion of outstanding bank credit to sick industrial units is accounted for by the large sick industrial units i.e. sick industrial units, individually enjoying bank credit of Rs. 1 crore and above from the banking system. It is also worth noting that while the number of large sick industrial units has almost doubled, the outstanding bank credit in such units increased more than two folds during the period 31st December 1976 to 31st December 1981. While a more severe pattern emerges in the case of sick small scale units*, sick units falling in the medium* category show a decline both by number and by outstanding bank credit for the last 3-4 years period for which the relevant data are available (Table-1).

* While 'small scale unit' is a unit as per the Ministry of Industry, Government of India's policy statement, a 'medium scale unit' is a non-SSI unit which enjoys credit of less than Rs. 1 crore from the banking system.

TABLE - 1 MAGNITUDE OF INDUSTRIAL SICKNESS

(Rs. in crores)

		As at 31st December					
		1976	1977	1978	1979	1980	1981
(A)	Total outstanding bank credit to all sick(a) industrial units	N.A. (N.A.)	N.A. (N.A.)	1,194.53 (N.A.)	1,622.55 (22,366)	1,808.66 (24,550)	2,025.54 (26,758)
(B)	Of which						
1.	To large(b) sick industrial units	608.75 (241)	858.45 (289)	1,060.96 (344)	1,158.48 (378)	1,324.47 (409)	1,478.84 (422)
2.	To medium(c) sick industrial units.	N.A. (N.A.)	N.A. (N.A.)	N.A. (N.A.)	202.33 (1,013)	178.42 (992)	187.63 (994)
3.	To SSI(d) sick units	N.A. (N.A.)	N.A. (N.A.)	133.57** (6,278)	261.74 (20,975)	305.77 (23,149)	359.07 (25,342)

Notes :

N.A. : Not available.

Figures in brackets denote number of units;

(a) The RBI has defined a 'sick' unit as one which incurs cash loss for one year and in the judgement of the bank, is likely to continue to incur cash loss for the current year as well as the following year and has an imbalance in its financial structure, such as a current ratio of less than one and a worsening debt-equity ratio.

(b) Large sick industrial units are those sick units individually enjoying aggregate bank credit of Rs. 1 crore and above from the banking system.

(c) Medium scale units are non-SSI units which have been granted credit facilities of less than Rs. 1 crore from the banking system. In the quarterly returns furnished by banks to the RBI, separate aggregate data in respect of all SSI sick units, in respect of individual large scale sick units and aggregate data for medium and large scale sick units only are furnished. Thus separate data on medium scale sick units are not collected from banks. Aggregate data on medium scale sick units are derived by subtracting from the combined data on large and medium scale sick units, the data on large scale sick units.

(d) SSI units are units as per the Ministry of Industry, Government of India's policy statement.

* Relate to large sick industrial and small scale sick industrial units only.

** Excluding data from State Bank of India and United Bank of India.

Source : Sick Industrial Units Division, Industrial and Export Credit Department, Reserve Bank of India.

Besides the banks, the term lending institutions, viz. IDBI, IFCI and ICICI also have funds locked up in the sick industrial units under their portfolio. As per the parameters followed by the term lending institutions, a unit is considered sick if the unit has (i) continuous cash losses for a period of two years or continued erosion in the net worth, say by 50%; (ii) continuous defaults in meeting four consecutive half-yearly instalments of interest or principal on the institutional loans; (iii) shortfall in the margin for bank advances and persistent irregularities in operations on the unit's credit limits with banks and (iv) mounting arrears on account of statutory and other liabilities for, say, a period of one/two years.

Thus as per the parameters followed by the term lending institutions, 224 units under their portfolio were sick as at the end of December 1981 with outstanding amount (excluding interest thereon) of Rs. 364 crores. If interest element is also added, the amount of outstanding loan to 224 sick industrial units in the portfolio of financial institutions becomes Rs. 440 crores as on 31st December 1981. It may be added that an increase both in number and outstanding loans to sick industrial units in the portfolio of financial institutions is also observed over the period 31st December 1978 to 31st December 1981 (Table-2).

TABLE - 2 INVOLVEMENT OF ALL-INDIA FINANCIAL INSTITUTIONS (IDBI, IFCI & ICICI) IN FINANCING SICK INDUSTRIAL UNITS (DIRECT LOAN PORTFOLIO)

	(Rs. in crores)			
		As on 31st December		
	1978	1979	1980	1981
1. Total outstanding of all borrower units from the all-India financial institutions. (direct loan portfolio)	1,341.3	1,630.3	2,049.1	3,079.77£
2. No. of sick@ units in the portfolio of financial institutions	200	202	205	224
3. Amount of outstanding loans to sick units in the portfolio of financial institutions	248.7 (284.4)*	279.0 (318.5)*	300.7 (365.4)*	363.8 (439.7)*
4. Percentage of item 3 to item 1	18.5 (21.2)*	17.1 (19.5)*	14.7 (17.8)*	11.8 (14.3)*

@ Definition of sick unit as adopted by financial institutions :

- i) Continuous cash losses for a period of two years or continued erosion in the net worth, say by 50%;
- ii) Continuous defaults in meeting four consecutive half-yearly instalments of interest or principal on institutional loans;
- iii) Shortfall in the margin for bank advances and persistent irregularities in operations on the unit's credit limits with banks and
- iv) Mounting arrears on account of statutory and other liabilities for, say, a period of one/two year(s)

* Including interest.

£ Relates to end-March 1982.

Source : IDBI

2.6 While studying the magnitude of industrial sickness either across the states or across the industries, the greatest handicap was the **Magnitude of industrial sickness :** non-availability of state-wise or industry-wise statistics either relating to the number of all types (large, medium and small) of sick industrial units or outstanding credit of commercial banks or any other relevant indicator relating to all types of sick industrial units. The only **state-wise and industry-wise** readily available information in this respect was in regard to the large sick industrial units (i.e. sick industrial units, individually enjoying aggregate credit of Rs. 1 crore and above from the banking system). The Committee thus had to confine the study of magnitude of industrial sickness across the states and industries to the large units only. In this context, it may be added that large industrial borrowers constitute a dominant proportion in the industrial sector of the economy as a whole as also in the important individual industries, as seen in terms of their share of outstanding bank credit in the total outstanding bank credit to industry. The aforesaid share was more than 75% for all industries taken together and well above 50% for most of the eight industries in regard to which the industry-wise data is available, excepting Iron and Steel, in the case of which the share was low (Annexure II). In view of the importance (in terms of outstanding bank credit) of large borrowers in the industrial sector, it may not be very inappropriate to restrict the study of magnitude of industrial sickness to large sick industrial units only. The analysis shows that the outstanding credit of scheduled commercial banks to large sick industrial units as on 31st December 1981 was highest in the State of West Bengal, followed closely by Maharashtra, Tamil Nadu, Uttar Pradesh, Gujarat and Karnataka in that order (Annexure III). A similar trend from the year 1976 and onwards was also noticed. Industry-wise, the highest outstanding credit of scheduled commercial banks to large sick industrial units was in Textiles followed by Engineering and Electricals, Chemicals, Jute and Iron and Steel. These industries right from 1976, more or less continued to remain in the aforesaid positions, viewed in terms of outstanding credit of scheduled commercial banks to large sick industrial units in the respective industries.

2.7 The analysis of the magnitude of industrial sickness, as presented in the preceding paragraphs, shows that the outstanding credit of scheduled commercial banks to large sick industrial units is substantial and has increased over the last 5-6 years. This statement holds good in regard to state-wise **Observations on magnitude of industrial sickness** analysis, in regard to the eight industries studied, as referred to in paragraph 2.2, and also for all the industries taken together. For all types (large, medium and small) of sick industrial units taken together also the outstanding credit of scheduled commercial banks has increased from the year 1979 (from

which data is available) upto 1981. It may, however, be mentioned that in the corresponding period both the total number of industrial units (whether sick or not) and the outstanding credit of scheduled commercial banks to them, either state-wise or industry-wise, has also increased. The Committee is aware that industrial sickness is bound to prevail in a developing economy where technology is changing fast not only due to technological changes that are taking place all over the world, but because the available technologies are being adopted in the country in phases, depending on our developmental stage.

2.8 With the above backdrop what should be of concern is the relative increase in industrial sickness—relative in terms of time-span and/or relative in terms of other countries, industrialised and developed or in a developing stage as is ours. Like **Incidence of industrial sickness** wise, to know whether the incidence of industrial sickness has increased or decreased over time, a study of proportion of either number or outstanding bank credit or any other relevant characteristic of sick industrial units in all the industrial units will be desirable. As discussed earlier the available data on industrial sickness in the country is mainly relating to large sick industrial units and that too for a period of 6-7 years and in regard to all types (large, medium and small) of sick industrial units taken together for 3 years only. The Committee was thus constrained to restrict the study of incidence of industrial sickness to the aforesaid data.

2.9 The analysis shows that as on 31st December 1979, out of the total outstanding credit of scheduled commercial banks to industry, as much as 16.5% was accounted for by the sick industrial **Results of incidence of industrial sickness.** units of all types (large, medium and small) taken together*. This percentage declined marginally to 15.7 as at the end of December 1980 but crossed the level of 1979 to touch 16.6 by December 1981. Thus for all types of industrial units taken together we may at the most say that there is some indication that the incidence of industrial sickness has marginally increased. In the case of large sick industrial units, the incidence of industrial sickness at all-industry level varied between 12% to 14% for the period 1976 to 1981, both ending December (Annexure IV). The incidence of industrial sickness in the large industrial units, as on December 1981, was found to be very high in Jute; high in Rubber, Sugar, Iron and Steel and Textiles out of the eight industries (vide paragraph 2.2) studied. In some of the industries analysed, there is a clear trend towards increase in the incidence of industrial sickness over the years. As discussed in paragraphs 2.2 to 2.4, data collected from banks for certain specific purposes are used for the

* These results are derived from the data presented in Table-1 and Annexure-II

study of magnitude and incidence of industrial sickness. It is thus necessary that much emphasis on the magnitude of the results on incidence of industrial sickness need not be placed and it is only the broad trend over the period in the incidence of industrial sickness which may be taken into consideration.

2.10 In order to suggest effective steps to arrest the increasing incidence of industrial sickness and also to formulate various measures for rehabilitating the sick industrial units, it becomes necessary to study the various factors which normally contribute to the sickness of industrial units. It may be clarified that the Committee did not undertake any field survey to analyse the causes of sickness in the industrial units. The Committee, however, made use of the various available published/unpublished source materials for this purpose. These include research publications/books on topics of industrial sickness in India and abroad by individual authors or by certain institutions, the statistics available in the studies carried out by the RBI and studies of some selected sick industrial units for which information was made available to the Committee by the banks and financial institutions which were involved in the rehabilitation programme of the concerned sick industrial units. References to these source materials are made at appropriate places.

2.11 A broad analysis of the various known academic causes of industrial sickness, both internal and external as culled out from the available published research material*, is given below under broad categories :-

(A) INTERNAL CAUSES

(1) Planning

(a) Technical feasibility

Inadequate technical know-how
Locational disadvantage
Outdated production process

* These include :-

- i) ICICI, *Problem Projects and their Rehabilitation; Industrial Credit and Investment Corporation of India's Experience*, 1977.
- ii) S. K. Chakraborty and P. K. Sen, *Industrial Sickness and Revival in India — Essays, Cases and Debates*, 1980.
- iii) National Council of Applied Economic Research (NCAER), *A Study of Industrial Sickness*, July 1979.
- iv) Sudarshan Lal, *How to Prevent Industrial Sickness — Symptoms & Rehabilitation*, 1979.

(b) Economic viability

High cost of inputs
 Break-even point too high
 Uneconomic size of project
 Under-estimation of financial requirements
 Unduly large investment in fixed assets
 Over-estimation of demand

(2) Implementation

Cost overruns **resulting from**
 Delays in getting licences/sanctions, etc.
 Inadequate mobilisation of finance.

(3) Production**(a) Production management**

Inappropriate product-mix
 Poor quality control
 Poor capacity utilisation
 High cost of production
 Poor inventory management
 Inadequate maintenance
 Lack of timely and adequate modernisation, etc.

(b) Labour management

Excessively high wage structure
 Inefficient handling of labour problems
 Excessive manpower
 Poor labour productivity
 Poor labour relations

(c) Marketing management

Dependence on a single customer/single product
 Poor sales realisation
 Defective pricing policy
 Booking of large orders at fixed prices in an inflationary market
 Weak market organisation
 Lack of market feedback and market research

(d) Financial management

Poor resources management
 Faulty costing
 Liberal dividend policy
 General financial indiscipline
 Deficiency of funds
 Siphoning away of funds
 Over-trading
 Unfavourable gearing or keeping adverse debt-equity ratio

(e) **Administrative management**

Over centralisation

Lack of professionalism

Lack of feed-back to management (Management Information System)

Lack of controls

Lack of timely diversification

Excessive expenditure on R & D

Dividend loyalties (where the same management has interest in more than one unit, cases are known where promoters of limited companies who also own private ownership firms tend to look after the interests of the latter, often at the cost of the former)

Dissension within the management

Incompetent management

Dishonest management

(B) **EXTERNAL CAUSES**(a) **Infrastructural bottlenecks**

Non-availability of/irregular supply of critical raw materials or other inputs

Chronic power shortage

Transport bottlenecks

(b) **Financial bottlenecks**

Non-availability of adequate finance

(c) **Government controls and policies, etc.**

Government price controls नयने

Fiscal duties

Abrupt change in Government policies

Procedural delays on the part of the financial/licensing/other controlling or regulating authorities (Banks, RBI, financial institutions, Government departments, licensing authorities, Monopolies and Restrictive Trade Practices Board, etc.)

(d) **Market constraints**

Market saturation

Revolutionary technological advances rendering one's products obsolete

(e) **Extraneous factors**

Natural calamities

Political situation (domestic as well as international)

War

Sympathetic strikes

Multiplicity of labour unions

It may be mentioned that the causes enumerated above are only illustrative and not exhaustive. There might arise peculiar situations in which a particular unit or industry may fall sick due to any other reason/s also, which may not have found a place in the above analysis.

2.12 As discussed in paragraph 2.2, the SIUD in the IECD, RBI, is receiving periodical data from the scheduled commercial banks in respect of large sick industrial units financed by them (each unit enjoying an aggregate credit limit of Rs. 1 crore and above from the banking system). For the purpose of the meeting convened by the RBI, as referred to in paragraph 1.11, information was called for, from the banks on the causes of sickness of 378 large industrial units which were reported as sick as at end of December 1979 and a one time study was undertaken on the causes of industrial sickness. This cause-wise analysis of large sick units, based on the causes of sickness as per the opinion and perception of the banks shows that there are five main causes of industrial sickness. The table below gives a break-up of the number of sick units and the main causes therefor.

TABLE - 3 CAUSES OF INDUSTRIAL SICKNESS — STUDY OF 378 SICK INDUSTRIAL UNITS

Causes	As at end-December 1979	
	No. of sick units	Percentage to total
a) Deficiencies in management	197	52
b) Market recession and environmental factors	86	23
c) Technical factors and faulty initial planning	52	14
d) Infrastructural factors (power cut, shortage of critical inputs, etc.)	24	9
e) Labour trouble		2
Total	378	100

In analysing the causes of sickness, it should be borne in mind that sickness in an industrial unit cannot be attributed to a single and particular factor alone; but is the result of contribution of multifarious and multidimensional factors, either inter-related or independent of each other. So no rigidity in approach can be followed in singling out particular cause/s alone which would have made an industrial unit sick. This aspect has been clearly brought out from the analysis presented in the subsequent paragraphs.

According to the banks' opinion and perception of the causes of sickness, deficiency in management, which falls in the category of internal factors for adverse working of a unit, is the major cause of industrial sickness, in combination with other causes, affecting more than half of the 378 large sick units. On the other hand, out of the external factors, market recession and environmental factors made about 23 percent of the large 378 industrial units sick. The causes of sickness as discussed above, are as seen from the opinion and perception of the banks regarding the same. These perceptions are subjective and are, therefore, only indicative. Further, the banks for obvious reasons, might not have reported all the causes of sickness, such as delay in sanction/disbursement of loans by such institutions to the units, unfavourable policy and delay in decision by the different concerned agencies.

2.13 In order to pool the experience of the banks and financial institutions on the causes of industrial sickness, the Committee decided that the members of the Committee representing the banks and financial institutions should arrange to identify, in a meaningful way, the causes of sickness of the industrial units in their respective portfolios, where the corresponding banks and financial institutions have a lead role. Accordingly, information on the causes of sickness of 341 sick industrial units was made available to the Committee by its members representing the banks/financial institutions. Distribution of these 341 units according to various industry groups is as follows :

Industry Groups	No. of Units
Engineering, Electricals	
Iron & Steel	146
Textiles	44
Sugar	44
Chemicals	26
Jute	15
Paper	9
Cement	3
Leather	5
Pharmaceuticals	6
Glass & Ceramics	7
Hotels	8
Others	28
	<hr/>
	341
	<hr/>

2.14 Analysis of the causes of sickness of the 341 sick units is presented in Annexure V. It is observed that a number of causes in combination were responsible for making an industrial unit sick. It is also observed that some factors responsible for making a unit sick, occurred frequently in various units across the industry groups. The important causes of industrial sickness along with their frequency of occurrence (presented in parentheses) in the 341 sick units studied are given below :-

1. Management deficiencies/mismanagement/dissensions (222 units)
2. Marketing constraints/competitive market (99 units)
3. Shortage of working capital/liquidity constraints (81 units)
4. Power cuts (77 units)
5. Labour trouble/poor labour relations (76 units)
6. Raw materials shortage/non-availability (74 units)
7. Plant imbalance/frequent breakdowns/obsolete machinery (72 units)
8. Demand recession/fluctuating demand (57 units)
9. High cost of production (46 units)
10. Under-utilisation of capacity (44 units)
11. Government controls/adverse trading conditions/policy changes (32 units)
12. Delays in project implementation (30 units)
13. Cost overrun (29 units)
14. Lack of technical know-how (17 units)
15. Lack of quality control/inferior quality (11 units)

Of the important causes of industrial sickness enumerated above, the first 10 more dominant ones, arranged in the descending order of their frequency of occurrence are presented in Table-4, wherein the percentage of units (out of 341 studied) affected by these causes, is also given.

TABLE - 4 CAUSES OF INDUSTRIAL SICKNESS BY THEIR IMPORTANCE

Important causes of sickness	Percentage of units affected by the cause
1. Management deficiencies/ mismanagement/dissensions	65.1
2. Marketing constraints/competitive market	29.0
3. Shortage of working capital/ liquidity constraints	23.8
4. Power cuts	22.6
5. Labour trouble/poor labour relations	22.3
6. Raw materials shortage/non-availability	21.7
7. Plant imbalance/frequent breakdowns/obsolete machinery	21.1
8. Demand recession/fluctuating demand	16.7
9. High cost of production	13.5
10. Under-utilisation of capacity	12.9

It would be seen that management deficiency (which also includes dissensions in management, mismanagement, weak management and dishonest management) is the most widespread cause of industrial sickness, found in almost two-thirds of the 341 sick industrial units studied.

2.15 It could be expected that certain industries may be suffering from causes, specific to or more pronounced in such industries only apart from the common causes affecting all industries. Therefore, it would be important to go by the industry approach in identifying the causes of industrial sickness. Keeping this aspect in view, an analysis of the data of the 341 sick industrial units (which represented various industries), was also undertaken separately for individual industry groups. While the findings on the important causes of sickness in respect of industry groups for which there was a fair representation of sick industrial units out of the 341 mentioned above, are discussed in the following paragraphs, detailed results are presented in Annexure VI.

(a) **Engineering, Electricals, Iron & Steel Industry :** Almost two-thirds of the units under 'engineering, electricals, iron and steel' industry, suffered from management deficiencies/mismanagement/dissensions. The causes of sickness in this industry, coming next in importance were,

labour troubles/poor labour relations, shortage of working capital/liquidity constraints, marketing constraints/competitive market and power cuts. Demand recession/fluctuating demand, adverse trading conditions, plant imbalance/frequent breakdowns/obsolete machinery and under-utilisation of the capacity were other causes responsible for adverse working of the units under 'engineering, electricals, iron and steel' industry group.

(b) **Textile Industry** : In the case of 'textiles', while inefficient management was reported in as high as 73 percent of the sick units covered in the analysis, other important factors were imbalance in the plant/frequent breakdowns/obsolete machinery and demand recession. These factors reflected the poor maintenance of plant and machinery and lack of modernisation/diversification. These two factors were the reasons for poor working in almost half of the sick industrial units. Further, while nearly one-third of the sick industrial units were affected by power cuts, almost an equal number suffered because of shortage of working capital resulting in liquidity constraints. High cost of production and labour troubles were the causes affecting about a fourth of the units studied in the textile industry.

(c) **Sugar Industry** : While about two-thirds of the sick industrial units had inefficient management, shortage/non-availability of raw material (sugarcane) appeared to be a general phenomenon resulting in the adverse working of the sugar industry. A third important factor in this industry was the high cost of production.

(d) **Chemical Industry** : In the case of chemical industry, apart from deficiency in management, marketing constraints/competitive market was the second most important cause of sickness. Almost a third of the units suffered on account of under-utilisation of capacity. It is important to note that more than one-fourth of the units studied under this industry reported delay in project implementation, which in turn resulted in cost overrun. There were again difficulties with plant and machinery, mostly on account of defects at the installation stage itself or because the machinery installed was not suitable to Indian conditions — the industry being mostly of recent origin.

(e) **Jute Industry** : Marketing constraints and power cuts are found to be the two most important factors affecting the jute industry, while deficiency in management occupies the third place. Like the textile industry, the jute industry also has the disadvantage of old and obsolete machinery resulting in frequent breakdowns, including plant imbalance in more than a third of the units covered in the analysis.

(f) **Paper Industry :** Apart from management deficiencies, power cuts, plant imbalances/frequent breakdowns and cost overruns were the factors each affecting about one-third of the units in the paper industry. Further, a fifth of the units studied, suffered from each of the factors such as shortage of working capital, labour trouble, delays in project implementation and raw material shortages.

2.16 The analysis in the preceding paragraphs shows that there are specific causes of industrial sickness affecting particular industries only, though there are also some general causes such as management deficiencies which has been found responsible in majority of industries as an important factor for industrial sickness. It has thus become imperative that such of the causes affecting the entire industrial fabric of the country have to be dealt with expeditiously and effectively to contain, if not, reduce the industrial sickness in a short period. Further, for any policy decision, it is also important that while the causes common to all the units belonging to an industry group, have to be tackled in a general manner, those specific to a particular unit are to be tackled individually on the merits of each case.

2.17 The Committee, in order to understand various facets of industrial sickness such as causes of sickness, actions taken for the revival and the constraints in the successful implementation of the rehabilitation programmes etc., desired to have case studies of a few sick units which were rehabilitated/were under rehabilitation schemes. Thus, the Committee, through the good offices of its members from the banks and financial institutions, had obtained information relating to brief history, causes of sickness, packages of rehabilitation, etc., for 18 sick industrial units (each enjoying an aggregate financial assistance of Rs. 5 crores or more), which are rehabilitated/were under rehabilitation by the institution concerned on its own and/or in consortium with other banks and financial institutions. These case studies were selected under the following three categories while keeping in view due representation across industries and regions :

- (a) story of success,
- (b) story of failure, and
- (c) a unit falling in between the above two categories, where there is scope for improving the rehabilitation efforts so as to resuscitate it, possibly in a shorter span.

2.18 A cause-wise analysis of the aforesaid 18 case studies shows that technical factors and managerial factors are the most important causes of industrial sickness; 15 and 14 out of the 18 units studied are affected

by these causes respectively (Annexure VII). While the financial factors contributed to the sickness of half of the units studied, infrastructural factors and environmental factors were next in importance. It may be pointed out that the factors enumerated above are not mutually exclusive but are overlapping, i.e. more than two of them simultaneously contribute to the sickness of the industrial unit, as is evident from Annexure VII. Out of the managerial factors, ineffectiveness/inefficient management is the most important cause, followed by poor labour relations/labour troubles. Under-utilisation of capacity is found to be the most prominent reason of sickness under the technical factors. Less than half of the 18 sick industrial units studied, suffered from erratic power supply/power cut (infrastructural factors) while high debt service charges/interest rates (financial factors) were reported by more than one-fifth of the units. In 2 out of the 18 units studied, the reasons for sickness are identified as non-availability of timely finance from the banks and financial institutions. Taking into account, all the reasons of sickness for the individual units, it is observed from the analysis of the selected 18 case studies that the number of causes of sickness varied between the sick industrial units studied.

2.19 In its efforts to understand the causes of industrial sickness, the Committee also took note of the results of an internal study on the subject, conducted by the RBI. The aforesaid indepth study on the causes of industrial sickness and other associated aspects was based on 15 randomly selected large sick industrial units, i.e. each with a credit limit of Rs. 5 crores and above and which had not been financed by any term lending institution. The 15 large sick industrial units were selected by the procedure of random selection from a total of 60 such units in the list of 410 medium and large sick units, available with the RBI. The selection was done in such a way that the units selected, by and large, had a fair representation across the industries and also across the states of the country with due weightage to the industries/states in which the incidence of industrial sickness was high. Thus, out of the 15 units studied, 6 are located in Maharashtra, 5 in West Bengal, 2 in Tamil Nadu and 1 each in Rajasthan and Uttar Pradesh. Industry-wise, 2 units each belong to 'cotton textiles', 'engineering', 'jute textiles', 'rubber products' and 'manufacturing of batteries'. One unit each is selected from the 'sugar', 'glass', 'cement', 'chemical' and 'cigarette and tobacco' industries. The basic sources of data for the analysis on causes of sickness used in the aforesaid study are the various records/reports relating to the selected units, supplied by the banks and financial institutions to the RBI on different occasions, which by and large, though not uniformly, include (i) viability reports, (ii) reports of consultancy services/consultants, (iii) inspection/study reports of inter-institutional teams, (iv) agenda papers and minutes of

the proceedings of various meetings of the financial institutions/banks with or without promoter/management of the unit and (v) details of packages of rehabilitation, their implementation including reports on the working of the units, etc.

2.20 The results of the study (Annexure VIII) show that a number of causes, by their interplay, are responsible to make an industrial unit sick; no doubt, inefficient management, technical problems including frequent breakdowns, labour trouble and demand recession, are the factors, each of which in combination with other causes is found to have affected the working of more than half of the selected units. This would indicate that the causes of industrial sickness brought out in the afore-said study by the RBI broadly tally with those perceived and reported by the banks (c.f. paragraph 2.12.). A third important finding of the study is that most of the units fall sick either after a period of 25 years of incorporation (mainly because of obsolescence or lack of modernisation, etc.) or in their infancy stage (within 5 years of incorporation).

2.21 Taking into account the findings of all the studies discussed in the preceding paragraphs, a broad generalisation regarding important causes of industrial sickness emerges. It is observed that the factor most often responsible for industrial sickness can be identified as 'management'. This may take the form of poor production management, poor labour management, poor resources management, lack of professionalism, dissensions within the management or even dishonest management. It, therefore, follows that most effective schemes of rehabilitation must be geared up to tackle this aspect in order to achieve the desired results. After management, marketing constraints and demand recession are the other important factors due to which a unit is not able to survive in a highly competitive market. Obsolescence of machinery due to lack of modernisation or poor maintenance may result in frequent breakdowns and technical problems. This is another factor in the order of importance, which causes sickness of units. It is perhaps, because of this, that the states of West Bengal and Maharashtra which were the earliest to industrialise, show relatively high incidence of sickness.

The labour factor comes next in the order of importance. Either due to poor labour relations, inefficient handling of labour problems, excessive manpower, or prolonged strikes, etc., an industrial unit may be rendered sick. Non-availability/inadequate quantities of critical inputs, such as power, essential raw materials, etc. are other factors which are rather important causes of sickness in industrial units. Another factor

which must be mentioned is liquidity constraint or inadequate availability of funds. This may be due to inefficient resources management. It is also to be noted that a number of causes, by their interplay, are responsible for making a unit sick and all the causes affecting a unit have to be considered in the package of rehabilitation for successful and quick rehabilitation of the sick industrial unit under consideration. It is no doubt realised that any scheme of rehabilitation would necessarily involve the identification of the specific factors causing sickness in the particular industrial unit and steps would have to be taken to eliminate these factors. Further, since most of the sick industrial units are found to have fallen sick either after a period of 25 years of incorporation or in their infancy stage (within 5 years of incorporation), monitoring of units belonging to these two vital periods of sickness proneness, assumes further importance.

2.22 There could be a view that the causes of industrial sickness presented in the preceding paragraphs may not be the real or basic causes and that at least some of them may be the result or at best the indicators of industrial sickness. According to those holding this view, the real causes of industrial sickness are to be found somewhere else and that industrial sickness, by and large, arises from the institutional frame-work and the policy issues. Since the study on the above aspects was outside the purview of the Committee and since no authenticated analyses on the aforesaid aspects are available, the Committee is not in a position to have its views on the above aspect.

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CHAPTER III

VIEWS OF THE REPRESENTATIVE BODIES OF INDUSTRY AND TRADE, LABOUR, BANKS AND FINANCIAL INSTITUTIONS

One of the terms of reference of the Committee is "to identify in a general way, what are the concessions which should normally be made by the various agencies involved in the revival, including management and workers, and in that context, whether sick industrial units should be burdened with obligations like payment of minimum bonus and implementation of various wage awards, etc. which may be having adverse effects on the rehabilitation programmes" (item (v) of Memorandum dated 14th May 1981). In this context as mentioned in Chapter I, the Committee held discussions with the representatives of Chambers of Commerce, Trade and Industry, Labour Associations, Indian Banks' Association and chairmen of commercial banks and financial institutions to have the benefit of their views on the various issues involved. The views of the various organisations are summarised below. Copies of each of the questionnaires issued to the aforesaid bodies are furnished at Appendix III.

Views of Labour Representatives

3.2 On the issue of contribution by workers in rehabilitation efforts, by way of granting exemption to the sick industrial units, say for a limited period, from the implementation of various wage awards (existing as well as prospective) and from the obligation of payment of minimum bonus, reduction in wages, postponement of annual increments, modifications in service conditions, etc., specially in respect of units incurring cash losses, the representatives of labour were of the view that any proposal of this nature would not be justifiable for various reasons. The standard of living of the workers, unlike those in management, generally is near starvation level and the quantum of wages does not leave the workers any 'cushion' to make sacrifices specially, when the cost of living index is going up. If at all any sacrifices are to be made by the workers, then a provision for neutralisation for the increase in the cost of living should be provided. Where due to force of circumstances, workers have to make the necessary sacrifices lest the sick industrial unit be closed down thereby causing the workers to lose their jobs, the nature and quantum of sacrifices should not be forced upon them, but on such occasions, the workers should be taken into confidence by the management who should convince them on the need for the sacrifices. The representatives of labour also made it clear that there could be no

generalisation in this regard ~~and concessions~~ and sacrifices, if any, must be considered on merits mutually acceptable to both the employer and the employees on a case to case basis. They were of the firm view that there should be similar sacrifices from the Government, management and others as part of the rehabilitation package. The labour organisations suggested the setting up of a 'Benefit Fund' at the national level to which recourse could be had as an alternative to, or in addition to, the sacrifices from the workers. Minimum bonus, being a deferred wage, is their statutory right and therefore, could not be compromised upon in the normal circumstances, but by force of circumstances they may have to agree in certain cases.

3.3 The representatives of labour desired that the question of rationalisation of labour force should be discussed with the workers and a workable formula on a mutually agreed basis should be implemented. Such a scheme must be accompanied by a programme of re-employment of the labour rendered surplus, through suitable schemes from the Government, after providing for the terminal benefits and other financial obligations arising out of retrenchment. Similarly, on the question of automation as one of the means of improving productivity and thereby overcoming sickness, it was expressed that the labour organisations were always for productivity and would not mind streamlining of work methods/norms. However, care must be taken to ensure that the matter is discussed with the representatives of workers on a case to case basis, that automation does not result in retrenchment and in case some labour is rendered redundant, they should be re-employed elsewhere through alternative schemes, as stated earlier. The labour organisations also made a passing reference to the Five-Year Plans based on national policy to create more potential employment of labour and emphasised that care should be taken that automation is introduced not with a view to retrench the existing labour force but to increase the production by retaining the existing labour.

3.4 On the question of whether multiplicity of labour unions in an industrial organisation could be a cause of its sickness, the labour organisations were of the firm view that this was not the case. It was pointed out that even when there was no willing agreement on certain issues between the various unions they still came to an understanding on any feasible rational scheme. They, however, felt that where more than one union existed, the management/Government should not choose between them and patronise any one particular union on political grounds; on the other hand, they could choose the union enjoying the support of the majority of workers, rather than the recognised one. In this

context, the representatives of labour also observed that Government itself seems to be interested in multiplicity of unions, as against the U.K. pattern of one union in one industrial unit.

Workers' participation in management 3.5 Expressing their views on the concept of workers' participation in management, they felt that workers should be involved in a positive way in the management right from the inception of the unit and not after it falls sick. The workers' participation need not be limited to one-third representation on the boards alone, but there should also be equality of status and involvement as regards the right to hire and fire and an equal say in other aspects, such as planning, implementation, purchases, marketing, etc., as in the case of the other directors. Such an arrangement, it was argued, will make the workers spontaneously come forward to make sacrifices for rehabilitation whenever warranted by circumstances. Where necessary, workers in a sick industrial unit should be given a majority of shares in the equity holdings.

Defaults by management 3.6 A view was expressed that there should be deterrent legislation by which funds misappropriated by the management could be recovered from the defaulting management and if necessary, by attaching the personal assets of the directors, so as to meet the legitimate financial obligations to the workers.

Views of Chambers of Commerce.

Causes of sickness 3.7 On the causes of sickness in the industry, the Chambers of Commerce felt that though it was difficult to generalise, one of the reasons could be the fear on the part of the management to disclose the true state of affairs of the unit lest their good-will/business reputation be affected. Other causes attributed to making a unit sick are : (i) lack of timely modernisation/machinery replacement, (ii) new industrial location policy, (iii) non-availability of adequate and timely working capital credit, (iv) price control and allied measures, (v) infrastructural bottlenecks, (vi) deficiencies in the functioning of canalising agencies, (vii) assessment of banks ignoring the realities of business fluctuations, (viii) delay in review of representations by the concerned agencies, (ix) recession, (x) compulsion to pay minimum bonus under the Bonus Act. (xi) deteriorating industrial relations and (xii) general managerial deficiency and misfeasance. It was also pointed out that a study on Capacity Utilisation in Indian Industry, prepared by the Tata Consultancy Services for the Associated Chambers of Commerce and Industry of India, reveals that under-utilisation of capacity in various segments of industry, is also a factor causing industrial sickness.

3.8 On the prevention of sickness, the Chambers of Commerce expressed that the measures would have to differ from case to case on merits. An important aspect emphasised by them related to the monitoring and follow-up of credit extended by banks and financial institutions; according to them, it was rather ineffective and required improvement. To encourage modernisation and replacement of machinery a demand was made for higher depreciation in the initial years, even up to 80% in the first year itself, so that when the time came to modernise/replace the machinery, units would be in a better financial position to meet the expenditure in time, thus preventing sickness. Creating a proper monitoring and control mechanism to identify potential weaknesses in marketing and technical areas through the services of qualified and experienced personnel for which a regular pannel might be built up was another means of preventing sickness in industry.

3.9 Regarding the difficulties (legal or otherwise) experienced at present in effecting a change in the management in cases where management failure or deficiency is a major cause of sickness, the Chambers of Commerce felt that special measures designed to enable speedier change of management, should have in-built safeguards for preventing any misuse/abuse by subjective consideration. When change of management in a unit becomes inevitable, the unit should be declared as 'sick' by the banks and the financial institutions and full particulars of such units forwarded to the Chambers of Commerce so that they may assist in effecting suitable merger or takeover. Of course, the co-operation of management of the concerned companies is an essential prerequisite; otherwise, the practical alternative would only be selective nationalisation. They felt that sections 203, 388-B and 388-C of the Companies Act provide adequate powers to the Government for effecting change of management; the law is thus quite adequate and should be made greater use of. According to them, amendments seem necessary in section 396 of the Companies Act, section 23 of the Monopolies and Restrictive Trade Practices Act and section 18A of the Industries (Development and Regulation) Act.

3.10 On the criteria for selection of units for rehabilitation, the Chambers of Commerce expressed that not all the sick industrial units need be revived. Where a unit is too sick to be revived either because of lack of demand for its products for various reasons, or where its technology has become outdated, the unit should be allowed to die, as is being done in some other countries. Any criteria, they felt, for takeover/rehabilitation/reconstruction of a unit should be based only on

economic considerations, except in cases where their continued functioning would be required in public interest. Otherwise, any continued assistance to economically unviable units would result in scarce funds being diverted from economically productive purposes, which would be counter-productive to the nation as a whole. Assistance should, therefore, be given only in cases where there is a possibility of rehabilitation within a time frame of 3 to 5 years. In the opinion of the Chambers of Commerce, the existing concessions in the packages of rehabilitation, are quite satisfactory. They, however, expressed that any further concessions with a view to effecting speedier rehabilitation should depend on individual cases, on merits. It was emphasised that the banks and financial institutions should take up the issues relating to industrial sickness forcefully with the Government to prevent sickness on a large scale. Another important factor relates to the need for strengthening of the equity base through the support of the banks and financial institutions in addition to the soft loans and other concessions being given at present by the IRCI and IDBI.

3.11 The Chambers of Commerce expressed that sacrifices from the management and shareholders in rehabilitation efforts would have to be considered on a case to case basis and where sacrifices are agreed to, these should be in equal proportions as between shareholders, banks, financial institutions, Government and other interests. Workers should also be persuaded to agree to wage cuts for certain periods, as it would be difficult to continue to meet their entire wage demands. Similar arrangements might be worked out with the professional management personnel as well, although they might have a preference to switch over to jobs in good companies if and when some sacrifices were demanded from them. Further, the Chambers of Commerce felt that any sacrifice from the management in the shape of dividend, commission or remuneration would not be of a sizeable magnitude, except for psychological considerations. Likewise, there might not be a scope for reducing the commission to selling agents, as they are answerable to their respective shareholders and in any case, they are third parties having only commercial relations with the units.

3.12 The existing legal provisions, the Chambers of Commerce felt, would be adequate for effecting speedy rehabilitation of sick industrial units, and as such, they were opposed to any additional powers being conferred on the banks, financial institutions and Government through a special legislation. As regards legal delays, they were of the view that Special Benches should be constituted to handle cases/matters relating to sick industrial units. The area where the existing legal provisions were felt to be inadequate relates to mergers, as in such

cases the benefit of the provisions of section 72A of the Income-Tax Act is not readily available to the companies, due to extremely cumbersome procedures and policies. Restriction on the mergers among MRTP companies and mergers involving subsidiaries and interconnected companies might be removed. It was also suggested that mergers should be only voluntary and not compulsory. The existing procedure on amalgamation is stated to be cumbersome and dilatory; hence the relative sections of the Act should provide for a declaration being issued either by the Central Government or in the alternative, by the Specified Authority to the effect that the amalgamation is in 'public interest' and fulfils the prescribed conditions. Another suggestion was, that an amalgamated company should not be required to invest its own funds in the rehabilitation of a sick industrial unit and such funds should come from the tax benefits arising out of the merger. In the opinion of the Chambers of Commerce, the prescription of 'minimum size' needs a review so as to encourage the takeover of a larger number of small scale sick industrial units. The other suggestions in this direction were that diversification should be permitted wherever required, accumulated carry forward losses should also be allowed to be set off irrespective of a time gap in the continuity of the business, no separate approval from MRTP Commission should be called for and the additional depreciation allowance should be made available to the amalgamated companies. In order to simplify the procedure/policy relating to the disposal of certain non-essential assets of a sick industrial unit, so as to utilise the sale proceeds thereof for meeting various obligations including those to the banks and financial institutions, certain suggestions were also made. These suggestions relate to amendments to the Urban Land Ceiling Act to permit disposal of land on the recommendations of the banks and financial institutions, etc. and amendments to the relative statutory provisions relating to Capital Gains Tax/Income-Tax Act permitting a set-off against accumulated losses.

3.13 To cut down the incidence of sickness at the stage of implementation of a project itself, which is often caused due to excessive overrun in preliminary and pre-operative expenses, it was suggested that the help of an outside financial consultant might be taken by the financial institutions for monitoring the signs of sickness since effective monitoring could help prevent such overruns. The banks and financial institutions should also revamp/gear up their information system to detect signals of sickness early. The Chambers of Commerce were opposed to the suggestion of setting up of a special fund for rehabilitating the sick industrial units at the national level with contributions from the healthy units as well. It was expressed that they were also not in favour of any quasi-judicial body being set up for dealing with sick industrial

units. They felt that any decision adverse to the management should be arrived at only after giving an opportunity to such management to present their side of the case.

Views of Representatives of Banks and Financial Institutions

3.14 The banks and financial institutions were of the view that it would be desirable to evolve suitable mechanism to detect sickness at the initial stage itself, especially when a number of units that are being set up, are likely to become sick before their commencement of production, for various reasons.

Detection of sickness

There is also a need to improve the standard of appraisal of a project, particularly at the pre-sanction stage and also effect close co-ordination amongst all the financial institutions. It would, therefore, be desirable to associate banks as well at the stage of appraisal of a project. The implementation of a project should also be closely monitored by the banks and financial institutions to regulate the expenditure as per the schedule, so as to avoid any large cost overrun and time overrun; where necessary, such monitoring could be done by consultants appointed by the concerned banks and financial institutions who should ensure timely receipt of periodical progress reports on the implementation of a project. The representatives of banks and financial institutions felt that if the Government could consult them before converting letters of intent into licences, it would be helpful to prevent, to some extent, the setting up of units which might eventually go sick.

3.15 One of the representatives of the banks desired that the statutory auditors should be required to send confidential reports to the concerned banks on the state of affairs of a company on completion of the annual audit. While the appointment of concurrent auditors to look into the day to day operations of a company might be considered on a case to case basis, there should be a compulsory stock audit. They stressed the need for the banks

Confidential audit reports & role of nominee directors

to obtain periodical operating data of a company to monitor its progress from time to time and also initiate suitable and timely remedial measures, wherever necessary, to prevent sickness. While emphasising the need for increasing the effectiveness of the role of nominee directors of the banks and financial institutions on the assisted companies, the representatives of the financial institutions felt that it would not be practical to expect the nominee directors to rectify all the deficiencies in the conduct of affairs of the assisted companies on their own. It has become necessary to extend the same immunity to the nominee directors of banks as is available to the all-India financial institutions like the IDBI and IFCI.

3.16 The banks and financial institutions should maintain a panel of consultants having the requisite expertise for preparing programmes of rehabilitation in respect of sick industrial units. In this context, it was suggested that the financial institutions could rely more on the technical consultancy organisations sponsored by the all-India financial institutions in various states for entrusting such a task.

3.17 The representatives of the banks and financial institutions expressed that the existing criteria being adopted to determine viability were regarded as reasonable and adequate. There was, however, a feeling that the time-frame for rehabilitation should be reduced. In case a unit is not found viable on commercial basis, banks should not be asked to continue holding operations solely on considerations of public interest. In fact if efforts to revive a unit or even merge it with a healthy one do not succeed, it should be allowed to close down. Any concession made available should not be extended beyond the rehabilitation period, which should not normally be longer than the time required to set up a new unit.

3.18 While mentioning of the constraints in rehabilitation, attention was invited to the rather cumbersome and lengthy procedures under the various acts such as the MRTP Act, I (D & R) Act, Companies Act, etc. and also to the lack of co-ordination and agreement among the various agencies such as the banks and financial institutions, Central and State Governments, etc. In order to ensure that the package offers the right quantity of concessions at the right time, it is necessary to have a spirit of understanding on the part of all the concerned agencies. There should also be adequate delegation of powers to the officers to take the necessary decision in the meetings held to finalise the packages of reliefs/rehabilitation. The promoters should bring in funds on soft terms, repayable only after the unit has been revived. Similarly, the management should accept cuts in perquisites and remuneration voluntarily. Personal guarantees of promoters might be insisted upon to ensure their continued and close involvement, although these cannot be considered as a panacea for all ills. Labour should be agreeable for appropriate sacrifices on their part and also for improving productivity. Multiplicity of trade unions should be done away with. Central and State Governments should agree to guarantee the loans where required and to defer the dues relating to sales-tax, octroi, power, excise, etc. They should offer timely help to overcome hurdles in procurement of raw materials, resolving issues with labour, etc. Further, necessary relief from payment of income-tax on the in-

terest held in Interest Suspense Account should also be extended to the banks and financial institutions.

3.19 The three simultaneous requirements for healthy growth of industry are that the machinery should be replaced before it becomes worn out, that there should be minimum expansion of **Modernisation/renovation** business turnover and production facilities should be made in order to cope with the continuing cost increases and that there should be progressive modernisation of plant and machinery, etc., to avoid its becoming outmoded and uncompetitive in a highly competitive situation. As such, the need for modernisation/renovation is even greater now in the context of growing industrial sickness. It was observed by the banks that the Soft Loans Scheme of the IDBI, inspite of its laudable objectives, could not attract a good number of units to avail of the concessional facility. Further, the present taxation provisions relating to depreciation, etc., are based upon the old traditional system which has failed to take into account the need for setting aside adequate sums of money to cope with a series of important developments, viz., constant improvements in machinery, high rate of change in technology, rapid and continuing inflation, etc.

3.20 The representatives of the banks and financial institutions expressed that they encounter several difficulties in bringing about change in management as the methods available are time consuming and often efforts are made by the management **Difficulties in effecting change in management** to thwart their endeavour in this direction. They enumerated the various difficulties in effecting a timely change in the management of a sick industrial unit. In order that the process of change in the management might be smooth, the following suggestions were put forth for consideration by the Committee :

- (i) Each financial institution which has been set up by virtue of a statute, should be vested with adequate legal authority to intervene in the management of an assisted unit and bring about a change in the management, if need be. For this purpose, the existing provision in the IFC Act, 1948 and the SFCs Act, 1951 should be amended and enlarged and similar powers should be made available to institutions like the IDBI, LIC, GIC, UTI, etc.
- (ii) Suitable amendments may be considered either in the Industries (Development & Regulation) Act, in terms of which it might be possible for the Central Government or IDBI to effect such changes in the management of a sick industrial unit as may

be considered necessary by them so as to safeguard the interests of assisted concerns as also of the public, notwithstanding the provisions contained in any other law for the time being in force.

- (iii) Section 408 of the Companies Act, 1956 should be amended in such a manner that the interests of the public financial institutions and the shareholders or lenders are adequately safeguarded. For this purpose, a provision in section 408 could be added, more or less on the following lines :

“If a public financial institution has granted financial assistance to a company or is a shareholder of the said company and is satisfied that the existing management of the company is oppressive or is conducting its affairs in a manner which is prejudicial to the interests of such public financial institution, then the Central Government may remove any or all the directors of the company and may also appoint such number of directors as the Central Government may, by an order, in writing specify as being necessary to effectively safeguard the interests of the company as well of the public financial institution”.

- (iv) Apart from the foregoing suggestions, it is felt that a judicial or a quasi-judicial body might be set up by the Government either under the Industries (Development & Regulation) Act, or any other Act to which the proposals for effecting a change in the management or reconstruction, both financial and managerial, of sick industrial units, could be referred so that the existing procedures which are time consuming, are substituted by a simplified process. A permanent judicial or quasi-judicial authority so set up may be the final authority for approving the package/programme for the rehabilitation of the sick industrial units and it may also have jurisdiction for overseeing that the packages/programmes approved are being implemented without any inhibition.

3.21 The representatives of the banks and financial institutions were of the unanimous view that gross financial improprieties on the part of management should not go unpunished. The financial institutions felt that managements of sick industrial units are very callous in their approach to rehabilitation; they desire to throw the industrial units into the lap of the banks and financial institutions, and pressurise them to provide more and more funds. In this context, they wondered who should ultimately be responsible to nurse the sick industrial units —

**Black-listing
of errant
entrepreneurs**

whether banks, financial institutions, Central/State Governments, labour, or the management themselves. In this context, it was suggested that the data on errant entrepreneurs should be collected so that they could be black-listed and any further financial assistance could be judiciously denied to them. On the other hand, promoters with a proven record of creditworthiness could be provided necessary assistance in promoting new units without any hesitation. Keeping in view the roles that they are supposed to play, the financial institutions did not express themselves to be in favour of institutional purchase of sick industrial units or their shares.

3.22 It was pointed out that some of the provisions of the Industries (Development & Regulation) Act, are loaded against the banks and financial institutions. Pre-takeover liabilities are often not assumed by the new management. Even when these are assumed, banks have to render financial assistance in the post-takeover phase, pending eventual settlement, which is protracted. There is a case for streamlining the procedures under the Industries (Development & Regulation) Act for affording adequate protection to banks and financial institutions in respect of their advances before the takeover stage. It was further indicated that the policy announced by the Government regarding denotification of units taken over under the Industries (Development & Regulation) Act is also heavily loaded against the banks and financial institutions. It was suggested that they should be consulted and taken into confidence by the Government before any decision is taken in this regard and that advances of the banks and financial institutions to the units taken over under the Industries (Development & Regulation) Act should be guaranteed by the Government. Further, the compensation paid to the banks and financial institutions by the Government in the event of takeover/nationalisation of sick industrial units, is not only grossly inadequate but generally delayed with a low priority. Also, no interest is usually paid from the date of nationalisation.

3.23 The banks and financial institutions also emphasised the need for a panel of technical and other management specialists whose services could be drawn upon for managing the sick industrial units, as and when necessary. They were of the view that conceptually, it might not be advisable for them to compel an industry to modernise at any point of time. The decision whether to modernise, when to modernise and to what extent, should be primarily left to the management of the industrial units concerned. The banks and financial institutions could at best insist on the allocation of a part of the surplus generated by the units to a separate reserve account, to be used

for the purpose of modernisation, as and when the units felt the need for it.

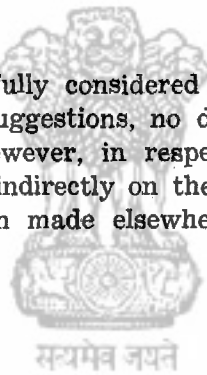
3.24 They also suggested setting up of a Standing Committee to which a reference could be made in case of disagreement, delay or default on the part of the participating agencies, in a rehabilitation programme, as experience suggests that arrangements in this direction have not been very satisfactory, resulting in further problems to the sick industrial units.

**Standing
Committee**

3.25 Regarding the proposal for setting up a National Fund for the specific purpose of assisting sick industrial units, the consensus was, that while the concept would be welcome, the banks and financial institutions should not be called upon to contribute to such a fund and that care should be taken through suitable guidelines to ensure that the resources of the Fund are not frittered away in meeting statutory liabilities of the sick industrial units.

**National
Fund**

3.26 The Committee carefully considered in detail the various above suggestions; some of the suggestions, no doubt, are not covered under the terms of reference. However, in respect of the suggestions which have a bearing directly or indirectly on the terms of reference, suitable recommendations have been made elsewhere in this Report wherever considered necessary.



CHAPTER IV

REVIEW OF VIABILITY CRITERIA AND PACKAGE OF REHABILITATION

One of the terms of reference of the Committee is : "To review the existing criteria adopted by banks/financial institutions in determining the suitability of a sick unit for revival and to recommend appropriate modifications therein, keeping particularly in view the need to have a reasonable time-frame for any programme of revival". (Item No. (ii) of Memorandum dated 14th May 1981).

While the existing criteria adopted by the banks and financial institutions in determining the viability of a sick industrial unit are discussed in the following paragraphs, the views and recommendations thereon of the Committee are presented in Chapter V.

4.2 The policy on sick industries enunciated by the Government of India on 15th May 1978, states that in considering the possibility of takeover of management under the Industries (Development and Regulation) Act, 1951, one of the factors to be taken into account, inter alia, would be the possibility of the undertaking becoming commercially viable in the foreseeable future. Viability of a sick industrial unit would be judged after taking into account the likely contribution to be made by labour, State Government, the banks and financial institutions for meeting its past liabilities and for viable operation of such unit after takeover. Subsequently, the revised policy on sick industries issued by the Government of India, on 6th October 1981, indicated that where the banks and financial institutions feel that, despite their best efforts it may not be possible to prevent an industrial unit from becoming sick or their efforts are unlikely to revive the sick undertaking, it should be reported to the Department of Industrial Development for a decision in regard to nationalisation of the unit or otherwise. In taking a decision about nationalisation of the sick industrial unit one of the criteria to be kept in view was that the Administrative Ministry must be satisfied that the unit can become viable within a reasonable period of time.

4.3 The Standing Co-ordination Committee (SOC) of the Reserve Bank had inter-alia considered the question of viability at a special meeting in September 1980, and norms for determining the viability of an industrial unit, evolved by consensus between the banks and financial institutions, are as under :

**SCC's
Recommendation on
viability**

"A unit should be considered viable if it was in a position to service its debts, at a reasonable rate of interest which would be concessional but not below the minimum lending rate and in no case below the cost of funds to the banks, within a reasonable period, say, about eight to ten years."

4.4 Under section 72(A) of the Income-Tax Act, relating to amalgamation of a company, the viability of an amalgamating company is seen in terms of financial considerations by reasons of the **Ingredients of company's liabilities, losses and other relevant factors and viability** the discretion on this aspect is left to the Specified Authority to make a recommendation to the Government to take a decision on amalgamation under the said section. As per a study*, financial viability consists of three interdependent elements, of equal emphasis and weight, viz., profitability, liquidity and solvency which are represented by cash profit or loss, net working capital and net worth respectively. Viewed in another way, solvency and liquidity are the two vital organs of financial viability, and profitability its life blood. According to the aforesaid study, the status of financial viability, at a point of time, is a result of the status of these elements, but in the absence of any precise index which combines the individual status of the above referred three elements, the status of financial viability at any point of time is gauged by giving equal weight to the said three elements.

4.5 The Committee noted that the following are the existing broad measures of the packages of reliefs for the sick industrial units under **Measures the rehabilitation programmes of the banks and financial institutions :**

- (i) The irregularity in the cash credit account (after physical verification and valuation of current assets hypothecated to banks) is determined and converted into term loan and interest rate on such borrowings is decided on the basis of debt servicing capacity of the unit.
- (ii) The overdue interest is funded and its repayment is phased based on the future cash generation of the unit. In certain cases, the overdue interest is converted into debentures secured or unsecured or equity capital.
- (iii) Similarly, based on the future cash generation of the sick industrial unit, the repayment schedule in respect of the term

* National Council of Applied Economic Research (NCAER), *A Study of Industrial Sickness*, July 1979, pp 13 and 14.

loans is rephased. Wherever necessary, a further repayment holiday is allowed on merits.

- (iv) Based on the type of need of the unit, additional financial assistance, term loans and/or working capital is sanctioned to the sick industrial unit on merit.
- (v) The unsecured loan from the directors or promoters and/or their associates is frozen and made interest-free or the rate of interest is determined with provision for repayment thereof after redemption of the entire rehabilitation assistance.
- (vi) Surplus plants and equipments or other fixed assets not required in the future operation of the unit are sold after obtaining consent from the chargeholders thereon.
- (vii) Similarly non-trading investments, if any, are also sold off.
- (viii) Moratorium is usually granted on payment of interest, either on loans and borrowings or on part thereof. Similarly, moratorium is also granted on repayment of principal.
- (ix) Efforts are made to bring about improvements in the management and management control system. Efforts are often made to effect changes at the Board level by persuasion or by exercising the covenants of loan agreement in the absence of any statutory powers to do so. Further, introduction of adequate management information system in the unit is insisted upon so that the management could get a proper feed-back on the affairs of the unit and could also provide the necessary and timely guidance.
- (x) The banks and financial institutions reserve the right to restructure the Board of Directors of the assisted sick industrial units by appointment of institutional nominees. Similarly, in deficient functional areas, effective management is installed, particularly, the procedures of purchase/sales arrangement are streamlined.
- (xi) The unit is required to submit progress reports periodically to the banks and financial institutions. Besides, monitoring of the project/revival scheme through internal/concurrent auditors is introduced, with a view to keeping close watch on the performance of the unit vis-a-vis the projected operations.
- (xii) Services of expert consultants/industrial engineers, etc. are availed of to solve intricate problems of technique, technology, production, marketing, etc.

- (xiii) Arrangement is made with statutory authorities and creditors regarding phased repayment of arrears, statutory and/or other dues. Avenues are explored to obtain sales-tax loan normally free of interest from the State Government. Requests are made to waive the penalties, if any, imposed which would have otherwise affected the viability of the unit.
- (xiv) Measures are taken to rationalise the labour force, if the non-viability of the unit is due to surplus labour or low productivity of labour.
- (xv) If the unit's financial position reveals serious imbalances due to heavy accumulated losses, etc., efforts are made to bring about restructuring of the financial position, particularly secured/unsecured loans, through the process of write-off/conversion/fresh issue, etc., and by revaluation of assets, wherever feasible. Reduction of share capital and foregoing of preference dividend is suggested but normally the implementation of such matters is a long drawn affair. For the same reason, compromise with the depositors/trade creditors is not attempted as it involves dilatory process and legal hazards.
- (xvi) If the above measures fail to yield the desired results and the assisted unit loses its long-term viability, efforts are made to expand the unit's capacity or to diversify its products.
- (xvii) If the unsecured liabilities pose a problem about current viable operation of the sick industrial unit, arrangement is made to declare such unit as a 'Relief Undertaking' by the concerned State Government, wherever possible and necessary.
- (xviii) Until recently, the Central Government was being requested to take-over management of the sick industrial unit, if deemed necessary, under I (D & R) Act, 1951. The criterion for such take-over of a sick industrial unit was the employment of more than 500 persons in the undertaking and it having fixed assets of not less than Rs. 1 crore. However, in exceptional cases, such takeover was also considered necessary in the national interest. Since the announcement of the policy of the Central Government on sick industries in 1981, the take-over of management was rare, except when it was prompted to nationalise the undertaking on fulfilment of the condition precedents, viz. viability of the operation and satisfaction of public interest.

4.6 The Committee felt that, before considering alternate/revised definition of viability including in particular the time-frame for the rehabilitation programme it would be desirable to have first hand information about the various concessions/reliefs granted presently by the banks, financial institutions, Central and State Governments and other agencies in rehabilitation programme as also to assess their efficiency in speedy revival of sick industrial units being rehabilitated. The Committee, therefore, took up in-depth study of 18 sick industrial units for which rehabilitation programmes were implemented/under implementation. As discussed in paragraph 2.17, for these units data was specifically for, from the concerned banks and financial institutions.

4.7 On a review of the 18 sick industrial units, it is observed that the period of the package of rehabilitation (including repayment of term loans) was in some cases 8-10 years, but in some others it was 15 years, depending on the terms of the rehabilitation package. While a few of the 18 sick industrial units could be revived to normal health in a shorter period compared to that envisaged in the package of rehabilitation, in some others, a definite improvement in their working was noted while the package efforts were in the process of implementation. In a few others, the units have not responded as yet to the revival measures, either because the packages of rehabilitation were introduced relatively recently or there were other unanticipated inhibiting extraneous factors.

4.8 The analysis of the types of concessions/reliefs given by the banks, financial institutions, Central and State Governments, quasi-governmental bodies, etc., done on the basis of 18 case studies, indicates that numerous types of concessions/reliefs are made available to the sick industrial unit in the package of rehabilitation for its revival. While it is not possible to generalise the magnitude of such concessions/reliefs and assess readily their impact on the sick industrial unit, it is observed that in the case of the banks and financial institutions, who undertake the maximum sacrifices for the revival of such unit, the concessions most commonly offered are in the form of reduction in interest rates both on term loans and working capital and funding of accumulated interest, with or without interest on the same. While the involvement of the Central and State Governments in extending concessions/reliefs in rehabilitation packages of sick industrial units is relatively small and to a few units only, in the case of State Governments such concessions are in the form of reduction in sales tax, finance tax, royalty

and electricity tariff, etc.; reliefs in terms of excise duty, non-interest bearing loans were generally the concessions coming from the Central Government. In some other cases, guarantees from the Central and State Governments were received against additional assistance by the banks and financial institutions. In a number of cases the promoters of such units were required to bring in additional funds in the form of unsecured deposits either with or without interest or on reduced rate of interest as part of the packages of rehabilitation.

4.9 In the package of rehabilitation scheme, it is provided that depending on the projected cash flow of the sick industrial unit, all the term loans including the funded portion of interest, etc., will be repaid by the sick industrial unit to the concerned institutions during the period covered under the package. The repayment schedule is drawn on the basis that about 75% of the surplus cash generation of the sick industrial unit will be utilised towards repayment of the term loans, which would normally ensure a comfortable level of 1.33:1 to 1.5:1 for the conventional Debt Service Coverage Ratio.

4.10 The RBI, in the course of its various instructions to the banks, has emphasised that once a sick industrial unit is considered potentially viable and a decision is taken to nurse it, it **RBI guidelines** may become necessary to consider reduction in margin and rate of interest, and rephase repayment schedule or amortise irregular portion of outstanding advance for recovery in a phased manner from out of the future cash generation of the concerned sick industrial unit. It is also made clear that wherever banks encounter situations in which they themselves are not able to provide the required assistance to sick industrial units, the banks should refer such cases to the IDBI for looking into the particular sick industrial unit's problems and drawing up a package of necessary measures for rehabilitation purpose.

4.11 When a sick industrial unit is identified as a potentially viable unit, it becomes necessary to prepare and implement an objective and purposeful package programme for its rehabilitation. In this context the Committee applied its mind on the term of reference, viz., "To identify the main constraints in the matter of rehabilitation of sick units, the problems faced by banks/financial institutions involved and to suggest remedial measures including amendments to various statutes". (Term of reference No. (iii) of Memorandum dated 14th May 1981.)

4.12 The various legal constraints in the different statutes that stood in the way of smooth and speedy rehabilitation of sick industrial units were considered and appropriate remedial measures including amendments to various statutes have been covered in the Interim Report of the Committee as discussed in Chapter VI. Other indirect legal constraints in the expeditious and successful rehabilitation of the sick unit, such as relative provisions under the Income-Tax Act, Urban Land Ceiling Act, Monopolies and Restrictive Trade Practices Act and Foreign Exchange Regulation Act, are also dealt with therein.

4.13 For identification of the main constraints in the matter of rehabilitation of sick industrial units, the Committee has mainly relied on the experience of the banks and financial institutions on the various constraints and difficulties faced by them in the matter of rehabilitation as conveyed to it during their deliberations in the various meetings of the Committee.

The Committee also took into consideration the views (presented in Chapter III) expressed by the representatives of trade, industry and labour organisations on the various hindrances which stood in the way of successful and expeditious rehabilitation of sick industrial units. The Committee has also utilised the information related to packages of rehabilitation, concessions, etc., given in regard to 18 sick industrial units, as discussed in paragraph 2.17, which were at various stages of revival. Likewise, an internal study conducted by the RBI of 15 large sick industrial units, each enjoying aggregate bank credit of Rs. 1 crore and above, as discussed in paragraph 2.19, also provided valuable information about the constraints in the way of successful implementation of the package schemes for revival of sick industrial units. The difficulties/constraints other than legal for the successful and expeditious revival of sick industrial units emerging out of various deliberations of the Committee and from the various sources referred to above, are discussed in the following paragraphs.

4.14 It is noted by the Committee that more often than not, symptoms of approaching sickness of an industrial unit are diagnosed at a very late stage at which any rehabilitation effort may become futile. Therefore, timely detection of symptoms of incipient sickness is an essential requisite for formulating a successful nursing programme, wherever considered necessary, at the stage of incipient sickness itself. The banks and financial institutions should have their own internal guidelines on the parameters, for timely diagnosis of the incipient sickness in an industrial unit. The Committee is of the opinion that no rigid definition of incipient sickness of an industrial unit may be laid down.

Each bank and financial institution, based on the financial data received from the borrowers as also from its day to day knowledge of its clients should be in a position to frame suitable guidelines for the purpose. It is considered necessary that some element of flexibility should be left with the banks and financial institutions. Another related problem is the difference of opinion between the banks and financial institutions about classification of the unit under 'sick' or 'incipient sick' categories whenever a package scheme is to be prepared jointly. Thus, it may be observed that delay in the detection of sickness of an industrial unit and disagreement on the same between the banks and financial institutions in turn, act as a hurdle in the timely formulation and implementation of a rehabilitation package. The Committee recommends that whether it is a consortium method of finance or multi-agency financing, there should be periodical exchange of information on the industrial unit, between the different agencies on a mutually agreed basis. In order to facilitate exchange of information about the borrowers, the banks and financial institutions may prescribe a common format for obtaining the necessary periodical operational data of the industrial unit and also prescribe as one of the terms and conditions of financing that the information in the prescribed format should be supplied by the borrowers to all the financial institutions. If, however, any single bank/financial institution desires to have any additional information in respect of its special type of loan given, e.g. foreign exchange, against personal guarantees of the directors, etc., it will be at liberty to call for such additional information as may be required, which should also be shared with other financial institutions, especially when the additional information thus called for throws out alarm signals in respect of incipient sickness of the industrial unit.

4.15 The Committee observed that quite often there are other considerations which compel the banks and financial institutions to carry on the rehabilitation programme irrespective of whether the sick industrial unit is considered viable or not on commercial basis.

4.16 In order to continue the operations of such sick industrial units it becomes obligatory on the part of the banks and financial institutions to extend the necessary finance to them. Likewise, State Governments which are mainly concerned with the question of sustaining employment opportunities expect the banks and financial institutions to continue to finance the sick industrial units, whether such units are viable on commercial basis or not. The Committee would like to reiterate that rehabilitation of a sick industrial unit should be taken up by the banks and financial institutions only if it is considered viable on commercial basis. The Committee also feels that the banks and financial institutions should not be made to

bear the burden of rehabilitating such sick industrial units in the name of socio-economic or public interest unless the Central/State Governments and other Government agencies also take up a reasonable portion of the sacrifices. It is also essential that the monetary sacrifices made by the banks and financial institutions are well protected by the Central/State Governments.

4.17 According to the Committee, the time-frame of 8-10 years in some cases of sick industrial units, and even longer upto 15 years in some other cases, adopted in the packages of rehabilitation is unduly long and has to be narrowed down so as to make it more purposeful and effective for speedy rehabilitation of the sick industrial units. It was keeping this aspect in mind that the consensus of the Committee, as discussed vide item (a) of paragraph 5.10 was that the period for rehabilitation of a sick industrial unit under a rehabilitation package should have an outer limit of 7 years.

4.18 The packages of reliefs evolved and adopted by the banks and financial institutions are generally on the lines discussed in paragraph 4.5. The Committee is of the view that the prevalent packages of rehabilitation need to be on more systematic, scientific and objective bases, so as to involve all the agencies in the packages. Thus, as recommended in paragraph 5.11, while it is imperative that each case, being unique in its own way, should be considered for the package of rehabilitation on its merits, the packages in general should be guided by specific norms as indicated therein.

4.19 The Committee observed that in certain cases, difference of opinion was perceptible between the banks and financial institutions on the nature and magnitude of sacrifices/concessions to be undertaken by them in the packages of rehabilitation of the sick industrial units. The various issues on which difference of views had arisen related to pooling and sharing of securities, ranking of charges, sharing of cash losses, providing additional finance, concessional rates of interest for such finances, repayment schedule, etc. It was also observed that even after agreeing for providing the requisite additional finances/concessions in the package of rehabilitation of certain sick industrial units, the banks and financial institutions could not stick to their commitments or the agreed finance/concessions were made available in dribblets which affected rehabilitation of the sick industrial

units to a considerable extent. All these factors resulted in delays either in evolving a suitable rehabilitation package or in expeditious implementation of the same. These constraints in the way of expeditious and successful rehabilitation of the sick industrial units along-with recommendations of the Committee on the same are discussed in detail in sub-chapter 10.E.

4.20 In certain cases, it becomes essential to change the existing management or take over the management of such sick industrial units by the banks and financial institutions. Finding an alternate suitable management thus becomes the responsibility of the banks and financial institutions, wherever a decision is taken to remove the existing management, which is not an easy task. In some other cases involving litigation, the existing management of the unit is forced to be changed through an order of the Court. The change in management is not known in time to the banks and financial institutions, as they are not parties in such litigations. The new managements in a few cases act in connivance with the previous managements and may not be serious about rehabilitating the sick industrial units. The non-availability in time of suitable alternate management for the sick industrial unit, makes the revival efforts of the banks and financial institutions all the more difficult. The Committee's recommendations in this regard are made in sub-chapter 10.L.

4.21 The Committee had noted that in many cases, the existing managements, after agreeing for the package of rehabilitation of the sick industrial units, were callous in their approach towards the rehabilitation programme, and they were more interested in starting new industrial units with fresh financial assistance from the banks and financial institutions. The Committee recognises that in quite a number of cases sickness in industrial units is due to reasons beyond the control of the management and any unqualified compulsion imposed to rehabilitate such units can only be at the cost of other industrial units in which, too, the banks, financial institutions and others have equal stake. There are also limitations imposed by other statutes, e.g. section 370 of the Companies Act, which limits investment in other companies, etc. However, it cannot be denied that the managements have a responsibility in helping the sick industrial units under their group to rehabilitate at the earliest. The recommendations of the Committee in this regard are given in sub-chapter 9.C.

4.22 The Committee was apprised that in some cases of rehabilitation of sick industrial units the labour, by and large, do not normally relish introduction of modified work systems, automation and even rationalisation of labour. There is also vehements opposition wherever concessions/sacrifices from labour either by way of reduction/temporary freezing of wages or reduction/postponement of bonus, etc., are called for. The Committee had discussions with various representative bodies of workers on these aspects and the gist of the same is presented in Chapter III. The Committee feels that labour is not always averse to modifications in the work procedure and automation provided they are essential. Labour is also willing to undertake some sacrifices for the revival of a unit when all concerned including management make sacrifices, provided it is taken into confidence and assured of adequate reward later. The Committee is of the opinion that co-operation of labour is a major step in the successful rehabilitation of a sick industrial unit and the Committee's recommendations in this behalf are given in sub-chapter 9.D.

4.23 A point was made by a representative of a trade union that sickness in most cases is due to lack of adequate attention on the part of management towards maintenance of machinery as also due to improper utilisation of funds meant for rehabilitation. It has been earlier mentioned that one of the important causes of sickness of a sick industrial unit is poor maintenance of plant and machinery which in many cases has also become obsolete (Paragraph 2.21). For the success of revival of sick units, the Committee is of the view that proper maintenance and replacement of plant and machinery at appropriate time, including its modernisation, wherever called for, are a must. The Committee's recommendations on modernisation are discussed in sub-chapter 10.A.

4.24 Proper end-use of the financial assistance provided by the banks, financial institutions and other agencies for rehabilitation of sick industrial units requires an elaborate monitoring and counselling system. Commendable efforts have already been made in this direction by the Central Government, RBI, banks and financial institutions, etc. The policy guidelines on sick industries, recently issued by the Government of India require that the banks and financial institutions should further strengthen the monitoring system including the information system by insisting on periodical returns from the assisted industrial units as also from their nominee directors. It was further required that the Industrial Development Bank of India should establish a separate cell to

examine and analyse these returns and reports and the results of the analysis be made available to other financial institutions and the Government for necessary corrective measures/action that may be called for. The Committee, through mail questionnaire, obtained information from banks on the set-up and qualifications, etc., of the personnel posted in their special sick units cells. An analysis of this information is provided in Annexure IX. As per the review, since some banks do not have many large sick industrial units under their loan portfolios, they did not set up the cells. The personnel in these special cells have to attend to other items of work in certain banks. A very insignificant proportion of them are technically qualified or have sufficient experience of dealing with sick industrial units. While services of the personnel posted in the cells are used for the conduct of viability studies of the sick industrial units, on many occasions such studies are done either in conjunction with consultants or consultancy services; sometimes by the consultants only. This is in spite of the fact that some of the banks have expressed that such an arrangement is not always very effective for taking quick measures for the rehabilitation of sick industrial units. There is ample scope for improving the counselling and monitoring role of the banks in regard to the sick industrial units in their portfolio. The Committee is of the view that the banks may get this issue studied by institutions like the National Institute for Bank Management, for appropriate expansion and strengthening of the cells as may be considered necessary.

4.25 As far as the mechanism of price controls by the Government is concerned, the industries can be broadly categorised into two groups.

Role of administered prices in revival of sick units In the first category are those groups of industries, such as drugs and pharmaceuticals, where statutory price controls are operative. In a majority of these cases, there are periodical reviews and any escalation in costs would be brought to the notice of the Government for appropriate action. The second group of industries relates to those where informal price controls exist, as in tyres, tubes, bicycles, etc. In such cases, the price rise is being decided with Government approval. The recommendations of the Committee on this issue are given in paragraph 9.A.1.

4.26 The study on causes of sickness of sick industrial units as discussed in paragraph 2.21 shows that in some cases of sick industrial units, non-availability at the appropriate time and in adequate measure of the various infrastructural facilities like transport, coal, power, besides scarce raw materials, was one of the main causes for making the units sick. More importantly, these causes continued even when the sick industrial

units were placed under the packages of rehabilitation of the banks and financial institutions and as such the very factors responsible for sickness came in the way of successful rehabilitation of such units after they became sick. Provision of financial assistance alone by the banks and financial institutions in adequate doses without tying up of timely and adequate supply of the various infrastructural facilities will be of no avail in rehabilitating a sick industrial unit. The recommendations of the Committee are given in paragraph 9.B.1.



CHAPTER V

MODEL PACKAGES AND VIABILITY CRITERIA

From the review of prevalent criteria of viability and packages of rehabilitation of sick industrial units (presented in paragraphs 4.2 to 4.10), the Committee observed as under :-

Existing

**criteria of
viability and
packages of
rehabilitation**

(i) The existing criteria of viability of sick industrial units, evolved by the SCC, as discussed in paragraph 4.3 has a certain amount of subjectivity — probably unavoidable in determining the viability of an industrial unit.

Further, the emphasis seems to be more on the debt servicing capacity of industrial unit under rehabilitation programmes. In the Committee's view, while finance is not the only problem for determination of viability, the viability concept should have a broader perspective and have the interest of the public at large. The criteria should also aim at the potential strength and health of the industrial unit from a long term perspective and should enable the banks and financial institutions to pick up such industrial units for rehabilitation by applying certain basic standards of viability for the determination of which a suitable time-frame and uniform approach is necessary.

(ii) It would also be apparent from the term of reference No. (ii) of Memorandum dated 14th May 1981 (cited in paragraph 4.1), that modifications if any, needed in the criteria adopted at present by the banks and financial institutions in determining the suitability of a sick industrial unit for its rehabilitation, should particularly have a direct bearing on the need to have a reasonable time-frame for any programme of its rehabilitation. The time-frame would, of course, vary in relation to the quantum of monetary sacrifices made by the banks, financial institutions and other participating agencies.

(iii) The time span usually provided according to the existing practice for offering packages of rehabilitation (inclusive of period of repayment of outstanding long-term dues) is rather long in some cases. This increases the element of uncertainty unavoidable in any such exercise. Several controllable and non-controllable factors intervene due to policy and other changes. Administration of successive doses of finance, etc., over a long period and co-ordination raise a host of problems, often leading to frustration of efforts. In the view of the Committee, in an ideal case, the time-frame should not be longer than the time required for setting up a new unit and bringing it to the level of normal commercial operations. Under normal conditions, it is expected that a new industrial unit would reach such a level within 5 to 7 years from its inception.

(iv) A major portion of the sacrifices under the present system of packages of rehabilitation of sick industrial units is normally made mainly by the banks and financial institutions. Sacrifices on the part of the Central and State Governments, including quasi-governmental agencies, promoters, etc., towards rehabilitation of sick industrial units are called for only in certain cases. Further, excepting certain cases where shareholders are persuaded to reduce the equity capital, in general they are not directly involved in the rehabilitation efforts by taking on themselves some sacrifices; no doubt, indirectly they continue to forego equity dividend till such time the units are restored to normal health.

(v) Computation of sacrifices in packages of rehabilitation, is confined normally to those shouldered by the banks and financial institutions, even though in certain cases some other agencies might have undertaken sacrifices in the form of concessions/reliefs to the sick industrial units under the packages of rehabilitation. Also either during the operative period of a package or after rehabilitation of the sick industrial unit, some benefits may flow to the banks, financial institutions, Central and State Governments, shareholders, etc., depending upon the response of the sick industrial unit to the rehabilitation efforts. Such benefits may be in the form of funded loans and other term loans which, in turn, can be recycled at normal rate of interest to the same or other healthy units, payment of statutory dues and taxes, payment of dividend on preference and equity capital. Benefits accruing to the various parties involved in the package of rehabilitation of a sick industrial unit should also be taken into account side by side while estimating the total sacrifices involved in the rehabilitation of the sick industrial unit.

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5.2 With the above backdrop and with a view to finding out whether some alternative packages of rehabilitation involving variations in the nature and extent of sacrifices by the banks and financial institutions as also sacrifices from equity holders, would enable the sick industrial units to rehabilitate in a relatively shorter span of time, the Committee took up an exercise using various alternative models of packages of rehabilitation for three out of 18 sick industrial units already taken up for rehabilitation by the banks and financial institutions. The near optimum package of rehabilitation may be the one where the sick industrial unit could revive and rehabilitate (as seen from its strength in terms of being able to pay a reasonable dividend) in a relatively shorter time span and, its stock market strength improves (as measured in terms of market value of equity share) with the minimum amount of sacrifices. While the extent of sacrifices involved in alternative packages, when compared to the package agreed to/implemented by the banks and financial institutions (henceforth called

'initial package') would prove the better acceptability of the former, the dividend paying position would indicate the stage of complete rehabilitation of the sick industrial unit under the various alternatives considered. Similarly, estimates of the value of equity share should broadly indicate the level at which the strength of such unit would be assessed by the market, i.e. as would be viewed by the entrepreneurs and other investors in the capital market. If the sick industrial unit can come back on the dividend list and/or its share value improves, it would be easier for the sick industrial unit to raise further capital, when needed, in the market, term loans, etc., from the banks and financial institutions on normal terms because of its improved image, for meeting its requirements for modernisation, diversification or expansion.

5.3 The cases of three sick industrial units out of the 18 mentioned in paragraph 2.17 to be called here as Model Case Study-1, Model Case

Study-2 and Model Case Study-3, were thus studied for **Methodology** various alternative models of packages of rehabilitation.

The various alternative models of packages considered, the methodology and computational aspects of estimation and the results derived from the three Model Case Studies, are discussed in the following paragraphs. The terms and conditions of the 'initial package' of rehabilitation of each Model Case Study were taken as the first assumption for the exercise on computation of alternative packages of rehabilitation for the respective units. In the alternative model packages examined in the exercise, extent and scope of the concessions/reliefs of the 'initial package' have been modified so as to study the effect of such variations on the overall revival of the sick industrial unit. While some alternative assumptions incorporate higher doses of initial sacrifices by the banks and financial institutions, in some others, restructuring of the capital base is stipulated and a third category of assumptions relates to cases of involvement of the shareholders also in the package of rehabilitation.

5.4 The various alternative assumptions considered in the analysis are as follows :

(I) Further reduction by 1/2/5 percentage points in the interest rates on term loans/working capital accommodation over and above the concessional rates of interest agreed to in the **Assumptions** for the Model 'initial package'.

Case Studies

(II) Conversion of overdue interest on term loans/working capital to equity capital.

(III) Write-off of overdue interest on term loans/working capital.

- (IV) Conversion of certain portion (25/50/75 per cent) of term loans into equity capital.
- (V) Reduction in equity, existing at the time of the 'initial package', by 25/50/75 per cent respectively.
- (VI) Combination of assumptions (I) and (III) i.e. further reduction in the interest rate by 1/2/5 percentage points respectively, with simultaneous write-off of overdue interest.
- (VII) Combination of assumptions (III) and (IV) i.e. write-off of overdue interest and conversion of a portion (25/50/75 per cent) of term loans into equity capital.
- (VIII) Combination of assumptions (III) and (V) i.e. write-off of overdue interest and reduction (by 25/50/75 per cent) in existing equity capital.
- (IX) Combination involving postponement of overdue interest and simultaneously further reduction in interest rates by 1/2 (one/two) percentage points, respectively.
- (X) Combination involving postponement of overdue interest and conversion of a portion (25/50 per cent) of term loan into equity capital.
- (XI) Combination involving postponement of overdue interest and reduction by 25/50 per cent of the existing equity capital.
- (XII) Combination of assumptions (IV) and (V) i.e. the complex effect of conversion of a part (25/50/75 per cent) of term loan into equity capital and also reduction by 25/50/75 per cent in the equity capital, existing at the time of the 'initial package'.

As an extreme case, sale of fixed assets and realisation of the dues to the extent feasible — a step in the direction of liquidation of sick industrial unit, is also examined as a further alternative assumption. Thus, it may be seen that in all a total of 14 assumptions, viz. the 'initial package', 12 enumerated above and the one involving sale of fixed assets have been considered. These assumptions, in turn, result into as many as 34 sub-assumptions each of which is examined for the three Model Case Studies for this exercise.

5.5 For each of the sub-assumptions, projected balance sheet and cash flow statements for the period of the package of rehabilitation were first prepared. In cases where the debt service coverage ratio of the unit is found to improve as a result of a certain alternative package involving lesser outgo by way of debt payment obligations, it has been assumed that the sick industrial unit will be in a position to meet its repayment obligations in a shorter period, as compared to that envisaged in the 'initial package'. The repayment capacity in a year is taken to the extent that after such payments, the unit will have a reasonable closing cash balance. To examine as to when the unit will be in a position to service the equity holders, the accumulated losses are first adjusted from the profits as and when accruing and thereafter all the relevant items of appropriation. The value of equity share at the end-year of the package of rehabilitation is first estimated by two methods, viz. (i) the yield method and (ii) the assets backing method. The average of the two estimates is taken to represent the market value of the equity share of the sick industrial unit. The nature of sacrifices and the benefits, accruing or likely to accrue to the various financing institutions (banks and financial institutions), Governments (Central and State), other governmental agencies, other institutions, promoters and shareholders, etc., during the period of the package, were first identified for various sub-assumptions. These sacrifices and benefits in various years of the package period were then estimated and aggregated to obtain estimates of net sacrifices, after converting the same in terms of the present value by making use of appropriate discount rates so as to have comparable estimates of present value of net sacrifices for various sub-assumptions of the packages. A uniform time span of the period of the 'initial package' for a particular Model Case Study is considered.

5.6 For judging the merits/demerits of the alternative sub-assumptions of the package of rehabilitation for a unit, the estimates of the three parameters, viz. the dividend paying position, the value of equity share at the end-year of the package and the amount of net sacrifices involved in the rehabilitation of the concerned sick industrial unit, derived for the various sub-assumptions are compared with those of the 'initial package' of the unit i.e. by taking the 'initial package' of rehabilitation as the norm of comparison. The computations under the various sub-assumptions are based on the projected working of the selected units as estimated for the 'initial package'. The estimation has thus the underlying assumption; had the conditions been the same as envisaged at the time of the 'initial package'. The methods of estimation also have certain weaknesses such as the appropriateness of the various discount rates used and limitations of estimation of future market value of equity share,

which again do not necessarily reflect the real financial strength of a unit. It is in the above background that the results obtained under the various alternative packages have to be viewed.

5.7 The results indicate that in terms of time required for the rehabilitation of the sick industrial unit, the amount of net sacrifices involved for the revival and the value of equity share at the end-Results of the year of the 'initial package', any of the two alternatives, Model Case viz. assumption VI (i.e. further reduction in the interest Studies rates by 1/2 (one/two) percentage points respectively, and at the same time writing off the overdue interest) and assumption VIII (i.e. writing off the overdue interest and simultaneously reducing by 25/50 per cent, the existing equity capital) are better packages of rehabilitation for both the Model Case Studies-1 and 3 compared to other alternative packages examined. However, assumptions IX and XI i.e. those involving combinations of postponement of overdue interest (instead of writing off the same) with either further reduction in the interest rates by 1/2 (one/two) percentage points or reducing equity capital by 25/50 percentage points, respectively, provide equally good alternative packages in the case of Model Case Study-3. While the most ideal package comes through assumption VI, in the case of Model Case Study-2 package through assumption VII i.e. writing off the overdue interest and simultaneously converting a portion (25/50 per cent) of term loan into equity capital, also has merits. This unit is otherwise found to be in an unviable position, almost remaining insensitive to most of the alternative packages considered including the combinations of postponement of overdue interest with either further reduction in interest or reduction of equity. It may be recalled that assumption VI, while assuming writing off the overdue interest, also considers further reduction in the concessional rates of interest already allowed by the banks and financial institutions. Similarly, writing off the overdue interest and simultaneous conversion of term loan into equity capital are considered in assumption VII. As such, under both these alternative packages, most of the burden of sacrifices has to be borne by the banks and financial institutions only. It may be emphasised that under these alternative packages, though the financing institutions are to take greater sacrifices in the initial years, in the ultimate analysis, their sacrifices will turn out to be either less or in any case not more than what they have committed to in the 'initial package', in fact in many cases sacrifices are much less. Assumption VIII, while increasing initially, on the one hand, the sacrifices of the banks and financial institutions in terms of writing off the overdue interest, provides, on the other, for reduction in the existing equity capital. In this case, all the three criteria of a near ideal package of rehabilitation, viz. early dividend payment by the unit, less total net sacrifices of the parties in-

volved for the rehabilitation of the unit and high value of equity share of the unit at the end-year of the package are fully met. In fact, the quantum of sacrifices, either total or for individual financing institutions are much less than that of the 'initial package'. If the sacrifices are to be kept low, at least initially, by postponement of overdue interest instead of writing off the same as a term of the package, it is seen that the scheme may be beneficial only in certain cases, depending upon the financial structure, including the amount of overdue interest, the conditions of the package, etc., of such units. It is worth mentioning that the exercises on the Model Case Studies do not take into account the benefits which the Government will have in the form of various levies and taxes including income-tax, once the unit starts earning profits and becomes liable to pay tax. Such benefits may be considerable in a longer time span. Likewise, the sacrifices that the workers and sundry creditors i.e. suppliers of goods and services, depositors and other creditors, etc., may be required to make are not considered for simplicity of the exercise.

5.8 The exercises on the three Model Case Studies have demonstrated the following important aspects :

Important aspects of Model Case Studies	<p>(a) that out of a number of alternative packages of rehabilitation considered, it is possible to select one, which with certain concessions, will enable a potentially viable sick industrial unit to rehabilitate (including repayment of outstanding dues) in a reasonably short time span of about 5 to 7 years while keeping the sacrifices of the institutions involved in the package of rehabilitation to the minimum possible. Such concessions could be from banks/ financial institutions in the nature of postponement by a few years/ further reduction of concessional interest rates by 1/2 (one/two) percentage points on working capital/term loans and conversion of 25/50 per cent of term loan into equity capital and reduction by 25/50 per cent of equity capital of the equity holders;</p>
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(b) that there may be certain chronic sick industrial units in the case of which any rehabilitation package, albeit reasonable to a limit, may not help the unit to be restored to its normal health and as such attempt to rehabilitate such cases may only result in wastage of fresh resources as well;

(c) that in the light of (a) and (b) above, it is possible to devise objectively the criteria to decide whether a sick industrial unit deserves rehabilitation efforts or it should be allowed to have its natural death. This, in turn, suggests that it could be possible to devise an objective definition of a viable industrial unit;

(d) that the near ideal packages of rehabilitation of sick industrial units coming from the results of the three Model Case Studies have two distinctive policy implications i.e. (i) whether the banks and financial institutions only should continue to take the major share of the sacrifices for the rehabilitation of the sick industrial units, or (ii) whether some part of the sacrifices can also be passed on to the promoters/owners/equity holders, who have the moral responsibility of bringing back the sick industrial unit to health. (Sacrifices from Government and other agencies are not considered here); and

(e) that while in certain alternative packages of rehabilitation, the initial sacrifices of the banks/financial institutions, may be high, in the ultimate analysis, the sacrifices for these institutions work out to be much less and in no case more than what they are already taking on themselves in the existing packages (initial package) of rehabilitation of a sick industrial unit.

5.9 Considering the nature and responsibilities of the banks and financial institutions as purveyors of credit on business principles and the need to maintain their soundness and trust, the Committee feels that viability of a sick industrial unit should be mainly judged on commercial consideration. Further the objective of fixing up the viability criteria for rehabilitation of a sick industrial unit should be to judge whether it would be economical to rehabilitate the sick industrial unit when compared to the quantum of sacrifices in monetary terms needed from the different participating agencies in its rehabilitation within a reasonable span of time of 5-7 years within which a newly incorporated industrial unit is in a position to stand on its own legs. The Committee also agrees with the view (discussed in paragraph 4.4) that profitability, liquidity and solvency of the industrial units are the three interdependent elements of equal emphasis and weight for determining the financial viability of an industrial unit. While deciding a reasonable time frame, a practical consideration kept in view was that in normal cases of healthy industrial units, the period for repayment of long-term dues by the unit is, by and large, kept at around 10 years.

5.10 Keeping all the above aspects in view and based on the results of the Model Case Studies vide paragraph 5.8 and after detailed consideration, the Committee has formulated the definition of viability as under :

“A sick industrial unit may be regarded as viable if it would be in a position, after implementing a package of concessions, spread over a period not exceeding seven years from the commencement

of the package, from banks, financial institutions, shareholders, labour, suppliers of goods and services or other creditors, as may be necessary, to continue to service its repayment obligations as agreed upon, including those forming part of the package, without the help of the concessions after the aforesaid period. The repayment period for restructured debts should not exceed ten years from the date of the implementation of the package and such a unit should be in a position to commence, if possible, declaration of dividend, both preference as well as equity, within a period of seven years."

5.11 The Committee makes the following recommendations in regard to the package of rehabilitation of the sick industrial unit :

Recommendations regarding package of rehabilitation (a) While offering the package of rehabilitation to a sick industrial unit, its financial implications from the point of view of possible sacrifices of all the agencies involved, including the shareholders, may invariably be studied by the banks and financial institutions. While the three parameters, viz. net sacrifices, equity servicing position and value of equity share for deciding an ideal package or near ideal package amongst the many considered in the Model Case Studies, may provide broad guidelines in this regard, they do not exhaust the various other parameters and the expediency of alternative packages. The banks/financial institutions may decide a package of rehabilitation under the broad umbrella discussed vide item (a) of paragraph 5.8, subject to the merits of the case, in such a manner that a viable sick industrial unit will be rehabilitated to normal health at the earliest, in not more than 7 years from the start of the implementation of the package of rehabilitation while keeping the total sacrifices to the minimum. In this context, the position of declaration of dividend by the sick industrial unit has special significance and deserves special weightage as the sick industrial unit may be in a position to stand on its own legs in its own right either for augmenting share capital or floating debentures or for raising loans on the normal terms. Otherwise, frequent infusion of concessionary finance from the banks and financial institutions would be required to pep up such a unit time and again.

(b) In order to have an equitable sharing of sacrifices on a rational basis, the packages of rehabilitation in suitable cases may entail, as recommended vide item (a) of paragraph 5.8, conversion of term loan into equity capital, reduction of equity capital, postponement

of overdue interest, conversion of overdue interest into term loan and reduction in the concessional rates of interest wherever necessary, the extent of conversion/reduction/postponement may be considered on the merits of each case. Based on the strength of the results of the Model Case Studies, the Committee also recommends that in the interest of the unit, banks, financial institutions and also the public at large, larger initial doses of concessions (which as discussed earlier, work out to be much less in the ultimate analysis), either by further reduction of interest rates or postponement of the overdue interest by the banks/financial institutions on merits may be desirable for quick rehabilitation of the sick industrial unit within the time frame of seven years as stipulated in (a) above. The Committee also suggests that sacrifices be demanded to the extent feasible from management, depositors, sundry and other creditors, Governments and workers so as to make the sacrifices not only more equitable and broad based but effective in helping the sick industrial units rehabilitate faster and reduce correspondingly the sacrifices to the extent possible on the part of the banks and financial institutions. The Committee is, no doubt, aware that in the present scheme of rehabilitation programme of sick industrial units by the banks and financial institutions, the shareholders and sundry creditors are not involved in view of the legal aspects and time taken in such process. Further, since the stake of the banks and financial institutions, both as lenders and often also as equity holders is substantial in most of the cases of sick industrial units, the sacrifices on the part of the other shareholders and creditors, would be relatively insignificant.

(c) The Committee is convinced that for the effective implementation of the reconstruction/rehabilitation programme, removal of existing legal and other procedural constraints is a vital necessity since reduction of equity capital may form an essential ingredient for an ideal or near ideal package of rehabilitation in the case of certain sick industrial units depending on the merits of each case.

(d) Viability (as defined in paragraph 5.10) should always be a paramount consideration before taking up any scheme for rehabilitation of sick industrial units, as the latter involves financial implications like write-off and on the top of it, grant of additional loans from the banks and financial institutions.

(e) No doubt, the Model Case Studies have shown that under a suitable package of rehabilitation of a sick industrial unit, it would be possible for the unit to service its equity after meeting statutory

and other obligations and after making repayments of its term loans, etc., the same does not imply that dividend need not be distributed by such unit once it comes out of the red and before all institutional long-term dues are fully discharged. The Committee further recommends that as and when warranted, within the time frame of seven years for the rehabilitation of the sick industrial unit, depending on the merits of the case and the financial position of the sick industrial unit, concessions extended for the revival of the unit may be reduced or withdrawn.



CHAPTER VI

SPECIAL LEGISLATION

The Legal Sub-Committee referred to in Chapter I, after having carefully examined the restraints in the various existing laws which are applicable to rehabilitation of sick industrial units, felt that :

- i) The remedies as available in terms of various existing statutes for reviving and rehabilitating sick industrial units are inadequate and dilatory, so much so that even many of the potentially viable sick industrial units could not be revived in time;
- ii) Many of the difficulties in rehabilitating sick industrial units arise because the various laws like the Companies Act, Monopolies & Restrictive Trade Practices Act, Industries (Development & Regulation) Act, etc., are not primarily meant to deal with the problems of sickness; even if a statute refers to sick industrial units or companies, the approach is sectoral and from its own limited angle rather than being based on a co-ordinated view. In such a situation, it is necessary to get out of the multiplicity of the existing laws and procedures and draw up a special legislation which will enable speedy and effective action to be taken for rehabilitation of the sick industrial units. Such a legislation can create a special body exclusively devoted to rehabilitation of sick industrial units, which step would ensure unified approach and speedy and time bound decisions;
- iii) Making of amendments to existing laws in their application to sick units as an alternative to the special legislative measures may not achieve the desired objectives because it would require a large number of amendments, substantive as well as consequential, in all such statutes;
- iv) Since various Acts have separate objectives, some of the amendments might not fit in their general schemes. A unified approach and concerted effort is also necessary in the rehabilitation of sick industrial units and accordingly, it would be advantageous to have a special legislation dealing with sick industrial units.

6.2 Having examined the limitations of the existing legal frame work vis-a-vis rehabilitation of sick industrial units, in the Interim Report, Objectives of the Committee felt that the comprehensive special legislation, designed to deal with the problems of sickness, should provide for its objectives and basic parameters within

which it should operate, the remedies necessary for the rehabilitation of sick industrial units, the body which should provide these remedies its procedures and other incidental matters required to make such legislation effective.

6.3 While underlining the need for special legislation and before outlining its form and content, the Committee would like to emphasise that the special legislation should not divest the banks and financial institutions of their responsibility to tackle the problems of sickness of the industrial units assisted by them. These agencies would have to make efforts for the rehabilitation of sick industrial units within the ambit of the existing remedies and powers available to them under statute or by covenants. As a supplemental expedient, the powers conferred on some of them could be modified or enlarged and those without it, could be conferred such powers to meet the exigencies of their rehabilitation effort. Only when they fail, they would seek remedies under the proposed special legislation.

6.4 Having regard to the above, the definition of a sick industrial undertaking for the purpose of the special legislation as formulated by the Committee is as under :

"A sick industrial undertaking is an industrial undertaking which expression includes a company or a co-operative society owning the industrial undertaking as the case may be and which has all the following characteristics and also those as have been taken over and continue to be so taken over under the Industries (Development & Regulation) Act, 1951, namely :-

- i) the industrial undertaking incurs in the immediate preceding accounting year cash loss as disclosed in the audited or the proforma balance sheet that is to say the loss arrived at in the manufacturing/profit and loss account of such industrial undertaking after making provisions for all expenses, including interest as also accrued interest but without providing for any depreciation (in accordance with the provisions of the Companies Act, 1956) and transfers to reserves like Development Rebate Reserve, Investment Allowance Reserve, General Reserve, etc.;
- ii) the current ratio that is to say the ratio between current assets and current liabilities as disclosed in the audited or proforma accounts of the immediate preceding accounting year of such industrial undertaking proves adverse according to the prevalent commercial accounting practice; and

- iii) the accumulated losses of such industrial undertaking as at the end of the immediate preceding accounting year result in erosion of 50% or more of its net worth or in any erosion of its paid up capital."

For the purposes of this definition :-

- a) Net worth is the sum total of the Paid-Up Capital and Reserves other than Reserves earmarked for any specific purpose or those arrived at on account of revaluation of fixed assets but includes the balance at the foot of Profit and Loss Account of the immediate preceding accounting year of such industrial undertaking.
- b) Revaluation of the fixed assets in any form and that if any made in the immediate preceding accounting year or that proposed to be made for the current year shall not be taken into account.
- c) Paid-Up Capital is the actual amount received or deemed to have been received by such industrial undertaking in respect of its equity and preference share capital including the rights and bonus shares issued, if any, and the equity shares issued pursuant to the exercise of the right of conversion attached to loans or debentures.

6.5 Under the Special Legislation it is proposed that a special body may be constituted which will exclusively and expeditiously provide the necessary remedies for the rehabilitation of sick industrial units which are, or which are owned by, companies or co-operative societies in cases where the existing measures are not found adequate. This may be in the nature of a Board called the Board for Industrial Revival, dealt with in the next chapter.

CHAPTER VII

BOARD FOR INDUSTRIAL REVIVAL

The Board for Industrial Revival may be a quasi-judicial body and it will have the same powers as a civil court in passing orders and in matters relating to execution or enforcement thereof.

Set-up

7.2 The functions of the Board may be as follows :

i) To consider and if thought fit to sanction, with or without modification, proposals relating to any sick industrial undertaking for :

Functions

- a) change in or take over of management of the sick industrial undertaking;
- b) reconstruction, including restructuring of share capital and liabilities of the sick industrial undertaking;
- c) merger or amalgamation of two industrial undertakings, one of which is a sick industrial undertaking;
- d) leasing the whole or any part of the sick industrial undertaking;
- e) sale of the sick industrial undertaking as a running concern;
- f) take over of a sick industrial undertaking by purchase of shares by any other industrial undertaking;
- g) liquidation or dissolution of the sick industrial undertaking and if found expedient, purchase of its assets; and

ii) to attend to such other matters as may be notified by the Central Government.

7.3 The Board shall consist of a full-time Chairman and two full-time members drawn from specialised fields such as finance, accountancy, management, engineering and law, as may be appointed by Central Government. The Board may co-opt one or more members as it may deem fit.

Constitution

7.4 The Board may be free to adopt a summary procedure for its working and its decision in regard to the manner of revival of a sick industrial undertaking and other incidental matters shall be binding on all concerned parties. To ensure finality and speed, the Committee is of the view that the decision of the Board should be made non-justiceable except to the extent of writ and other jurisdiction of High Courts and the Supreme Court.

Pattern of working

Only such industrial undertakings as may be covered under the definition of a sick industrial undertaking formulated by the Committee as also such industrial undertakings as have been taken over by the Government under the I (D & R) Act, may be eligible for being referred to the Board. The Board may also be empowered to act suo moto.

7.5 The Board may ask the concerned parties to give their written submissions. This suggestion is being made to avoid undue delays which may be caused by continuous oral hearing or arguments. If the rehabilitation scheme contemplates merger of the sick industrial undertaking, the bank or the financial institution submitting the proposal should simultaneously forward to the Board the consent of the transferee unit. A time frame should be prescribed for the completion of formalities at various stages keeping in view the need for speedy revival. Proposals may also be submitted by the Central or State Governments. In cases of voluntary mergers, the proposals may be submitted by the concerned companies also. The Board may obtain the assistance of the IRCI as Nodal Agency with regard to the consideration of the proposals, etc., received by it.

7.6 If the Board decides that a particular sick industrial undertaking cannot be revived under the proposed scheme, a copy of its findings should be simultaneously sent to the Central Government.

7.7 If the rehabilitation scheme contemplates take-over of the management or possession of the sick industrial undertaking, such take-over has necessarily to be related to the other remedies with a view towards the eventual revival of the sick industrial undertaking.

7.8 During the period a proposal is under its consideration, the Board, if it considers necessary, with the assistance of the Nodal Agency (IRCI), can exercise certain powers such as suspension of onerous or unfair contracts and obligations and stay of legal proceedings relating thereto, appointment of directors and managers.

7.9 The rehabilitation scheme may be sanctioned by the Board with or without modifications within a period normally not exceeding three months from the date of receipt of the proposal. In exceptional cases the Board may, at its option and for reasons to be recorded in writing, extend the said period by another one month. The scheme as sanctioned shall be binding on the sick industrial undertaking, its creditors, members, banks and financial institutions and all other persons or authorities whose rights or interests are involved.

7.10 Under the proposed special legislation, the Board should follow the principles of natural justice and also proceed with the proposal expeditiously. The Board should follow its own procedures without being influenced by the procedures laid down in other statutes like the Civil Procedure Code, etc. The Board will have the powers of a Civil Court in passing orders and in matters relating to execution or enforcement thereof.

7.11 A draft of the special legislation is furnished in Appendix II.



CHAPTER VIII

RECOVERY OF DUES

Large amounts advanced by the banks and financial institutions to defaulting industrial units and other defaulting borrowers are locked up due to the delays under the existing legal procedure and process for recovery.

8.2 The Civil Courts are burdened with diverse types of cases. Recovery of dues by the banks and financial institutions is not given any priority by the Civil Courts. The banks and financial institutions like any other litigants have to go through a process of delays pursuing the cases for recovery through Civil Courts for unduly long periods. First the case has to be instituted in the Lower Court which, after issue of summons, receipt of pleadings, framing of issues, taking evidence — oral and documentary and giving hearings, pronounces its judgement. Against such judgement, provision is made for an appeal to Sub/District Court or to High Court if the appeal is from Sub/District Court. There can also be a second appeal or revision petition to High Court. On the decision of High Court the litigation can be taken to the Supreme Court under certain circumstances and thus have it prolonged. The progress more often gets bogged down through interlocutory petitions and stay orders from higher courts. Due to the delays involved in such elaborate process the interests of the banks and financial institutions are very often adversely affected. Attempts will, therefore, have to be made to reduce the impact of the arduous procedures presently obtaining for the recovery of dues insofar as the banks and financial institutions are concerned.

8.3 The Committee endorsed the views of the Sub-Committee referred to in Chapter I to examine and recommend the need for a special legislation for recovery of dues of the banks and financial institutions and recommends inter alia the enactment of a special legislation for such recoveries. The Sub-Committee drew upon the data and the views furnished by 18 nationalised banks, the SBI and its 7 subsidiaries regarding the number of suits instituted, amounts sought to be recovered and received and expenditure on the litigation available with the Ministry of Finance, Government of India as also the information regarding the above received from the IFCI, IRCI and ICICI. It was also noted that the IDBI had so far filed only one suit for such recovery. Data so collected are furnished in Annexure X. The views of the Sub-Committee are as follows :

- i) After examining the provisions contained in the Revenue Recovery Act, Public Demands Recovery Acts, Income-tax Act

insofar as it relates to recovery of dues, Co-operative Societies Act, the summary procedure provided for under Order 37 of the Civil Procedure Code and the judicial pronouncements in relation thereto, it felt that since the resources of the banks and financial institutions are backed by public deposits, public borrowings and budgetary allocations being public funds, the principle that the State should have a special procedure to enforce its own demands should equally be extended to the recovery of dues of the banks and financial institutions as well.

ii) Since the emphasis is on the recovery of dues, such a special machinery should apply to recovery of dues of the banks and financial institutions, from all industries (including small scale industries), whether normal or sick, and all other borrowers excluding the agriculturists.

iii) There could be three modes to recover such dues through special process, viz.

(a) to treat the dues of the banks and financial institutions as arrears of land revenue and to entrust the recovery to the State recovery machinery;

**Three
alternatives**

(b) to vest special powers in favour of the banks and financial institutions similar to those conferred on the IFCI and the SFCs under their respective statutes and

(c) to set up in terms of the special legislation, quasi-judicial authorities, functioning like administrative tribunals, exclusively devoted to adjudicate on issues relating to such recoveries. The relative merits of the said three modes are discussed in the following paragraphs.

iv) The first mode is to treat the dues of the banks and financial institutions as arrears of land revenue and to entrust the recovery to the State Revenue Authorities. It may, however, be noted that the state recovery machinery for recovering land revenue is already burdened with the recovery of a number of public dues. The said machinery has also to perform a number of other duties of the State. According to the Madras High Court*, the expression 'land revenue' has acquired a definite and well-understood meaning and it is not open to legislature, by fiction, to treat something which is not 'land revenue' as

* In the case of Venkataswamy versus Tamil Nadu SID Corporation (AIR 1981 Madras 318)

'land revenue' and to make law with respect to the same. In the light of the said observation, it would not be advisable to treat the dues of the banks and financial institutions as arrears of land revenue. Further, in view of the magnitude of the task involved, and the mounting arrears, it would not be advisable to entrust the task of recovery to the state revenue machinery.

v) The second mode is to vest special powers in favour of the banks and financial institutions similar to the powers conferred on IFCI and SFCs under their respective statutes for recovering their dues. While it is noted that certain SFCs have met with a good deal of success in making recoveries by invoking special provisions of the SFCs Act, the efforts of the IFCI in this regard to recover their dues from large scale units have not met with the same degree of success.

To confer powers on banks and financial institutions similar to those of IFCI/SFCs

vi) The third mode is to set up quasi-judicial bodies like administrative tribunals to deal exclusively with the recovery of dues of the banks and the financial institutions by following summary procedures. With the growth of modern administration, setting up of tribunals is being accepted as being inevitable. The number of cases being disposed of by tribunals in England is, perhaps, more than those by the civil courts. In France, there is a whole set of administrative tribunals under the system *Droit Administratif*. In India also there are tribunals for settling industrial, labour, income-tax, irrigation, revenue and service matters and co-operative tribunals for recovery of dues of the co-operative banks. Recognising the need for speedy settlement of issues by specialised bodies, the Constitution of India has made special provisions (Articles 323A and 323B) for settlement of certain disputes. In the light of what is stated above, it is recommended that the Central Government may set up a class of tribunals which would in a summary way but following the principles of natural justice, adjudicate finally, within a time-bound schedule, all matters in relation to recovery of dues of the banks and financial institutions. These tribunals should be manned by persons having specialised knowledge in the functioning of banks, financial institutions and industry. They should follow simple and summary procedures in accordance with the principles of natural justice without having to follow the ordinary procedures of Civil Courts. Besides, as in the case of other tribunals no court fee need be required to be paid. As the intermediation of lawyers except in suitable cases is usually

Special Tribunals

avoided in such procedures, the cost of proceedings can also be brought down considerably.

- vii) It is noted that a major hurdle relates to the requirement of obtaining permission of the competent authority under the Urban Land Ceiling exemptions Urban Land (Ceiling and Regulation) Act, 1976. Except in rare cases, where there is no excess land, the said permission will have to be obtained before creation of security. Under the said Act, the banks and financial institutions are permitted to hold properties of their own, whether the land is in excess or not, without the necessity of any permission. To enable institutions to obtain security over the properties of the borrowers/guarantors, the Urban Land Ceiling legislation may be amended to the effect that no permission will be required for creating the security in favour of the banks and financial institutions over the land.
- viii) There should be a special procedure in the legislation for creation of statutory charge in favour of the banks and financial institutions, by filing a declaration in the prescribed form, with the Registrar of Assurances, in whose jurisdiction the immovable properties (subject to the charge) are situate. Obtaining security by way of declaratory charge to secure bank advances to agriculturists over their properties was recognised and recommended by the Talwar Committee*¹ which has since been accepted. Such a provision to secure the advances of banks was also suggested by the Banking Laws Committee under the Chairmanship of the Late Justice P.V. Rajamannar.*² Further a Committee headed by Dr. R. K. Hazari (then Deputy Governor, RBI) in its report*³ to the RBI also recommended that there should be a simple charge by way of declaration termed as "GEHAN" in favour of co-operative societies. The said Committee also suggested that the charge so created in favour of co-operative societies might be assigned in favour of higher financing agencies for the purpose of obtaining necessary resources.
- ix) It is suggested that the proposed special legislation may provide for creation of such declaratory charge to secure all types of loans, advances and guarantees given/furnished by the banks and financial institutions. Where security consists of only mov-

*1. Report of the Expert Group on State Enactments having a bearing on commercial banks' lending to agriculture (published by the RBI in 1971).

*2. Banking Laws Committee's Report on Real Property Security Law, 1977.

*3. Report on Integration of Co-operative Credit Institutions finalised in 1976 (published by Agricultural Refinance & Development Corporation).

ables the creation of charge by way of hypothecation as presently obtaining will continue.

x) Provision may be made in the legislation for making variations of the terms as recorded in the said declarations and for recording satisfaction of charge by filing further variations-
satisfaction of declarations as may be prescribed.
declaratory
charge

xi) Broadly, the specimen of the format regarding creation of Format of charge may be as follows :
charge

- A. Name of the Lender :
- B. Name of the Borrower :
- C. Name of the Guarantor, if any :
- D. Loan/assistance :
- E. Payable on demand or as per repayment schedule or the Period of repayment :
- F. Interest rate etc. :
- G. Other terms :
- H. Schedules of properties charged :

EXECUTION

on behalf of
the lender

on behalf of
the borrower

on behalf of
the guarantor

xii) The rights of the charge-holders (which may also include the right to assign the security to other banks and financial institutions for obtaining finance/refinance to augment the resources of the charge holding bank) claims of charge-holders *inter se* and liabilities of the borrower/guarantor may also be specified in the legislation.

xiii) Stamp duty on such declaratory charge (it being a statutory charge) is not attracted and payable and provision may be made in this regard in the legislation. Further, provision may be made in the special legislation for levy of a nominal registration charge as appropriate. The provisions of the Indian Registration Act, 1908 will have to be suitably amended to provide for registration of declaratory charges with

Stamp duty,
Registration
fee

the concerned Sub-Registrar of Assurances and a new sub-section (1A) may be incorporated in Section 17 of the Registration Act.

- xiv) It may be noted here that the State Laws on Co-operative Societies, give priority by way of first charge, to a co-operative society, notwithstanding the fact that the charge in favour of the society might have been created at a point latter to the existing charges/mortgages of other creditors. Such an out of the way priority in favour of the banks and financial institutions is not being suggested by the Committee. However, it is necessary to ensure that the obligations of the banks and financial institutions *inter se* for sharing the distributable proceeds are adequately tied up through *inter se* agreements/arrangements. Such *inter se* agreements/arrangements should be treated as mere agreements and stampable and registerable as such. It was felt that the present practice amongst the banks and financial institutions viz. to enter into *inter se pari passu* or other arrangements amongst the banks and financial institutions themselves without the borrowers being made parties to such arrangements and obtaining from the borrowers subsequently, letters of confirmation in regard to such arrangements may continue, although some doubts have been expressed as regards the legal efficacy of such arrangements without the borrowers being made parties thereto. Suitable provision may be made in the special legislation for this purpose.

8.4 The constitution and functions of the Special Tribunals and ancillary matters in relations to the proceedings before them are given in Annexure XI.

- 8.5 It is noted that Banking Laws Committee* made certain recommendations regarding creation of mortgage by deposit of title deeds and registration of charges created by way of hypothecation of movables and it is understood that these are under consideration of the RBI. The above suggestions may be taken up by the RBI with the Central Government for implementation by amending the existing legislation or promoting new legislation.

**Suggestions
of Banking
Laws
Committee**

* Banking Laws Committee's Report on Documents of Title to Goods, 1978 and Report on Real Property Security Law, 1977.

CHAPTER IX

CONCESSIONS FROM VARIOUS AGENCIES

In addition to examining the existing legal provisions having a bearing on rehabilitation of sick industrial units and recommending two special legislations to facilitate (a) speedy rehabilitation of sick industrial units, as also (b) recovery of dues of the banks and financial institutions, the Committee particularly deliberated on the following two terms of reference, viz. 'to identify in a general way what are the concessions which should normally be made by the various agencies involved in the revival, including management and workers, and in that context, whether sick units should be burdened with obligations like payment of minimum bonus and implementation of various wage awards, etc., which may be having adverse effects on the rehabilitation programmes' and 'to make such other suggestions and recommendations which in the opinion of the Committee are expedient for speeding up revival of the sick units' (items (v) and (x) of the Memorandum dated 14th May 1981). Based on the various discussions and the views expressed by the representatives of trade and industry, labour organisations, banks and financial institutions, etc., as set out in Chapter III, certain recommendations having a bearing on speedy rehabilitation of sick units have been made by the Committee. It may be added that just as the phenomenon of sickness though common in a generic sense, appears in individual sick industrial units due to one or a combination of causative factors, the remedial measures too have to be a mosaic of selected measures constituting a package depending on diagnostic analysis of each case. The recommendations set out in the following sub-chapters are intended to serve to the extent feasible as aids to prevention of sickness as for instance modernisation, etc. and for cutting down administrative delays in implementation of package of measures so as to speed up the process of revival e.g. Working Group Concept.

9.2 As stated earlier, the reliefs/concessions forming part of a package are evolved, based on the requirements of a sick industrial unit and the problems faced by it as revealed by the diagnostic study. These reliefs, apart from involving monetary concessions from the banks and financial institutions, also require certain concessions to be extended by various agencies such as Central/State Governments, management, labour, shareholders, depositors, creditors, etc. It has been the general experience of the banks and financial institutions, as brought to the notice of the Committee, that at times while the necessary concessions from the banks and financial institutions are made available, the reliefs required from other agencies are not readily forthcoming; if at all forthcoming, they are not in adequate measure and at

**Sacrifices
relating to
the package
of rehabi-
litation**

the appropriate time, with the result that the programmes of rehabilitation of the sick industrial units cannot be carried out as per the original package. The Committee is, therefore, of the view that the present practice of the banks and financial institutions and also the Central and State Governments taking upon themselves varying degrees of sacrifices in the scheme of rehabilitation would be meaningful and justified, only if the other agencies including the shareholders and labour who have an equal responsibility in bringing back the sick industrial unit to normal health in the interest of all concerned, also contribute their mite in the package of rehabilitation. The reliefs/sacrifices expected from the different agencies responsible for rehabilitation of potentially viable sick industrial units are discussed below.

9.A. RELIEFS AND CONCESSIONS FROM THE GOVERNMENT

9.A.1 The Committee is aware that while specific concessions may be required in a few selected cases on merits, it may be difficult for the Central and State Governments to allow deviations on a case-to-case basis; to avoid the charge of discrimination **Central Government** any concessions extended by the Central and State governments are required to be applicable to a class of sick industrial units rather than to individual cases unless there is overriding public interest consideration in a particular case. To meet this requirement, it is suggested that such concessions may be made applicable to 'sick industrial units' as a class with clearly demarcated guidelines specifying the circumstances under which the concessions could be granted. The concessions envisaged from the Central Government are broadly listed below :

- (1) Exemption from Central excise, wholly or partly, for a period of time/deferment of collection or treating the dues as a loan repayable on the lines of sales tax loans from the State Governments.
- (2) Exemption from import duty, etc. on import of machinery, etc. for increasing/improving the production.
- (3) Income tax reliefs as discussed under paragraphs 10.I.1, 10.J.1. and 10.J.2 to banks as under :
 - i) Exemption from interest tax in case of sick industrial units.
 - ii) Exemption from income tax of amounts placed in interest suspense account.
- (4) Preferential allotment of canalised items to sick industrial units.
- (5) Deferment of provident fund/waiver of penalties, income tax and Employees' State Insurance dues and collection after suitable re-

phasing and ensuring at the same time that there is no deprivation of benefits to the retiring or sick employees.

- (6) Exemption from payment of minimum bonus under the Payment of Bonus Act for the limited period, though the amount may continue to form a contingent liability to be discharged when the sick industrial unit is in a position to do so.
- (7) Banks and financial institutions should not be asked to issue guarantee cover to the Central Government in respect of their dues e.g. provident fund, income tax, excise, etc.
- (8) In respect of sick public sector undertakings, 'defence oriented'/'export oriented' sick industrial units which, inspite of their non-viability, Government wants to be assisted on considerations of public interest, budgetary support through interest-free loans should be provided.
- (9) The pricing policy of the Government should be oriented so as not to aggravate the existing sickness.
- (10) Adequate marketing support should be given to sick industrial units, if necessary, by reserving a certain quota for a certain period for purchase by Government/semi-Government organisations. The sick industrial units should also be given price preference in the same way as public sector industrial units, as a measure of package.

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9.B. RELIEFS AND CONCESSIONS FROM STATE GOVERNMENTS

9.B.1 It was observed by the Committee that certain bottlenecks like power, transport and critical scarce raw materials also add to delay the process of rehabilitation of sick industrial units. The State Committee, therefore, recommends that the State Government should give priority in ensuring supply of the above inputs in adequate quantities through appropriate agencies so that the supply of these inputs should not normally stand in the way of speedy rehabilitation of sick industrial units.

- (1) Preferential treatment should be given to sick industrial units in respect of power supply and power supply should not be cut unilaterally to sick industrial units when they are under a process of rehabilitation, if the electricity dues are not paid on time. A realistic rescheduling of such dues should be worked out.

- (2) Concessions in power tariff should be made available for a specified period.
- (3) Exemption or certain concessions in the rate of sales tax/octroi duty and other duties/levies of the State/quasi-Government bodies should be given.
- (4) Speedier disposal of industrial disputes should be ensured. Where the rehabilitation schemes envisage rationalisation of labour, State Governments should use their good offices in the matter. Where in the larger interest of rehabilitation of sick industrial units closure of one or more units forms part of the package, expeditious permission for closure as required under the I (D & R) Act should be given.
- (5) Adequate market support for the products by strengthening the infrastructure should be provided.
- (6) Banks and financial institutions should not be asked to stand guarantees for the payment of dues of the sick industrial units to the State/quasi-Government bodies.
- (7) In respect of sick industrial units taken over by the State Governments, adequate budgetary support should be made to strengthen their equity base. Alternatively, State Industrial Development Corporations and State Industrial Investment Corporations might provide the requisite support.
- (8) Penal levies in respect of sick industrial units should be waived as a part of the package.
- (9) Exemption/concession from payment of stamp duty and registration charges with regard to creation of mortgage/charge by sick industrial units in favour of the banks and financial institutions may be made.
- (10) Declaration of sick industrial units as Relief Undertakings under the various States' Relief Undertakings Acts may be made as a matter of course.
- (11) Price preference in the matter of purchases as given to public sector industrial units should be given.
- (12) Expeditious permission under the Urban Land Ceiling Act, not only for creation of mortgage but also for sale of the mortgaged assets or excess vacant land to meet a part of the rehabilitation, should be given.

9.C CONCESSIONS AND SACRIFICES FROM THE MANAGEMENT

9.C.1 As shown in Chapter III, management is stated to account for 52% — 65% of the causes of sickness. While there may be a degree of subjectivity in this estimate, the dominant role of **Management** management cannot be over-emphasised. In the view of the Committee, there could be no two opinions about dealing sternly with delinquent or dishonest managements and in such cases changer or takeover of the managements cannot be avoided. In fact, the feeling of the Committee has been that this should be scrupulously done. In certain cases this may raise questions of compensation, etc. as provided in the Companies Act, but where the management is taken over under the I (D & R) Act, no compensation is payable. In the case of sick industrial units, there is hardly any justification for payment of compensation for loss of office. In other cases where the sickness is due to factors beyond the control of the management, it is nevertheless necessary for the management to co-operate in making whatever sacrifices are possible to match the sacrifices by other agencies, which form part of the package. The sacrifices may take the form of waiver or reduction of remuneration, etc., foregoing interest on any unsecured loans/deposits brought by self or friends and relatives, write off of loans and among others, bringing in fresh funds as may be decided under the package. It should also agree to the discipline imposed like reconstitution of management at the Board or operational level, appointment of finance/commercial directors/controllers, etc. So far as the professional management is concerned, it is difficult to quantify or delineate the type of sacrifices expected particularly, because such management is a scarce commodity; where there is apparent failure attributable to omissions and commissions, the loss of office may be the maximum end, but, in other cases perhaps a token or indicative gesture may suffice.

9.D. CONTRIBUTIONS AND SACRIFICES FROM LABOUR

9.D.1 The sacrifice on the part of labour may take various forms, since labour cost is a sizeable constituent of the cost of production and has to be proportionate to the norms in a particular industry. **Labour** Overmanning has been an obvious feature in several traditional industries in the grip of sickness. A purposeful rationalisation is the answer in such cases. Productivity, yet another important factor, has been considerably affected by indiscipline, go-slow, strikes, lock-outs, etc. Implementation of labour awards, etc. in the face of depleted and dwindling cash flow poses yet another serious problem. In these various circumstances, contribution from labour would

be expected by way of voluntarily agreeing to a scheme for rationalisation/retranchment of surplus staff, deferring or phasing out of retranchment compensation, etc., wage stabilisation, if not reduction, without insisting on increases, agreeing not to raise any fresh demand for the agreed period, increased productivity and productivity linked incentives, moderation of fringe facilities for a period of time, etc.

9.D.2 In this context, the Committee is fully conscious of the fact that in the absence of any scheme of workmen's redundancy or compensation fund, etc. in the country, any scheme of rationalisation/retranchment/voluntary retirement is bound to hit the labour hard and in the larger interest, including that of a majority of the labour force itself, it has to suggest what is best possible. The Committee, therefore, feels that whenever any suggestion on the rationalisation/reduction in the work force of a sick industrial unit is to be made as a part of the package programme, a proper work study preferably by a well known independent organisation like the National Productivity Council or well managed public sector undertakings should be desirable so that the workers would have confidence in the findings of such studies and would come out for the sacrifice on their part with fuller realisation of the inevitable. Wherever possible, participation of workers in such studies and evolution of a package programme for rehabilitation should be encouraged. Further, the established work norms available for any industry should be taken into account in these studies before determining surplus labour force. It is realised, however, that no generalisation as to the concessions to be given by the labour can be made and these would have to be determined on a case-to-case basis. The Committee also feels that where a sick industrial unit is under rehabilitation, there should also be an agreement with labour to increase production to the extent possible. This would make it convenient to review the position within a relatively short time, so that the sacrifices made by labour may be reviewed as early as possible. It should also be agreed that during the relevant period, labour will not resort to any direct agitational approach like strikes, go-slow, etc. which would hamper the process of speedy rehabilitation of the sick industrial unit. The period for which the sacrifices are demanded from labour should be specific and as far as practicable should also be with utmost understanding with them.

9.E SACRIFICES FROM SHAREHOLDERS

9.E.1 In the case of industrial units functioning normally, the shareholders can expect to receive their lawful dividends and also get the benefit of the appreciation in the market value of the shares. However, in the case of sick industrial units, the market value of the shares will be at a discount which

is an indirect loss to them not to speak of their entitlement of the dividend. In order, therefore, to retrieve the sick industrial units from sickness, the shareholders will have to voluntarily agree, as a part of the scheme of rehabilitation, to any scheme of restructuring resulting in writing down the value of the shares, share-exchange value in the case of merger or amalgamation of the sick industrial unit with another, pledge or deposit of their shares with the financing agency, if required and transfer of voting rights, etc. It need be remembered that when the sick industrial unit becomes healthy and normal, such sacrifices may be more than justified and perhaps the shareholders may expect handsome dividends and even bonus issues which could compensate them for their earlier sacrifices.

9.F SACRIFICES FROM DEPOSITORS

9.F.1 When an industrial unit is in good working condition and earning profit, the depositors get their interest regularly. When, however, such a unit has become sick and is under a scheme of rehabilitation, wherein sacrifices are being made by other agencies, it is but proper that the depositors will also have to sacrifice to a certain extent in their own interest, because as soon as the sick industrial unit becomes healthy and normal perhaps whatever loss has been incurred by the depositors may also be compensated wherever possible. The depositors should enter into an agreement with the sick industrial unit, foregoing the interest or agreeing to reduce the interest rate and rescheduling the repayment of their deposits till the sick industrial unit becomes healthy and normal.

9.G SACRIFICES FROM CREDITORS

9.G.1 Amongst the sundry creditors, the main category who constitute the bulk are the suppliers of raw materials and stores, etc. When the industrial units are in difficulty and face financial constraints, they resort to stretching payment to the creditors as a means to provide a source of financing cash loss. This course also offers a leeway for double and even multiple financing. On the other hand, if creditors' dues are not settled in time, they resort to stoppage of supplies, padding up the prices in their future supplies, charging heavy interest and carrying charges, etc. which all add to the burden on the sick industrial units in distress. In the case of non-payment, the sundry creditors may even go to the courts with winding-up petitions. While several States have now their Relief Undertakings Acts and can keep the creditors' dues frozen, it is always advisable that when packages are worked out, sundry

creditors are also made contributories to the packages wherever necessary. The sacrifices from them may take the form of agreeing to a phased liquidation of past dues and assurances for future supplies, settling their past dues after foregoing a portion thereof, desisting from filing winding-up petitions, extending co-operation at creditors' meetings to any scheme of reconstruction, merger, etc by consenting to the schemes and agreeing to certain fiscal and other concessions having regard to the circumstances of the concerned sick industrial unit.

9.3 Other related recommendations to serve as aids for prevention of sickness and for cutting down administrative delays in the implementation of packages of measures so as to speed up the process of rehabilitation of sick industrial units, are set out in the next chapter.



CHAPTER X

OTHER RELATED RECOMMENDATIONS

10.A. MODERNISATION

10.A.1 Obsolescence of plant and machinery as also of technology is recognised as one of the factors contributing to industrial sickness. The need was, therefore, felt to adopt some concrete measures **Modernisation** to enable the industrial units to overcome the backlog of modernisation, replacement and renovation of their plants and machineries so as to achieve higher and more economic levels of production and thereby improve their competitiveness in the domestic as well as the international markets. To this end, at the instance of the Government of India, the IDBI introduced its Soft Loan Scheme for Modernisation, in 1976-77. The scheme was operated by the IDBI and ICICI and covered five industries, viz. Cotton textiles, Jute, Cement, Sugar and certain Engineering industries. The scheme has since been extended to cover all industries. This scheme provides for exemption from the convertibility stipulations.

10.A.2. At present there is no legislation making modernisation compulsory. It is done purely at will. There are, however, certain provisions which enable an industrial unit to set apart certain funds for modernisation/replacement.

10.A.3. The Income-Tax Act allows provision for the replacement of assets through an allowable deduction for depreciation. Depreciation is a non-cash expense for which the assessee gets tax relief. There are however, no conditions attached to the grant of depreciation, either that it must be provided for in the accounts or that it must be separately invested for the specific purpose of utilising the amount for modernisation.

10.A.4. The tax laws also provide for the grant of an investment allowance in most cases. The grant of the allowance is subject to certain conditions, viz.

- (a) a reserve equivalent to 75% of the allowance has to be created in the year in which the allowance is claimed and,
- (b) the reserve has to be utilised within 8 years for acquiring new machinery or plant.

On similar lines, if depreciation is allowed for tax purposes to ensure that adequate funds are available for replacement of assets, then it is necessary to ensure that the depreciation so allowed is not distributed as dividend or otherwise utilised including acquisition of interest

in other companies. Such danger exists where an industrial unit follows the straight line method of depreciation, because the disposable profit as per the accounts is higher than the taxable profit (to the extent of the difference between the income-tax depreciation and the accounts depreciation) and there is no restriction on the payment of dividends, etc. out of this difference. One solution for this difficulty would be to provide that depreciation allowed for tax purposes should be restricted to the depreciation provided in the accounts. This may create some hardship for highly capital intensive industries which have a long gestation period since this would postpone the payment of dividend to an abnormally long date and thus make investment in such industries unattractive. The other solution would be to provide under the Companies Act that no dividend can be paid unless there is a transfer made from the disposable profits to a Deferred Taxation Reserve to ensure that the Reserve is equivalent to the tax savings arising from the aggregate difference between the depreciation allowed for tax purposes and the depreciation provided in the accounts.

10.A.5 While the Committee feels that the decision if and when to modernise is best left to the management themselves, it is equally important to ensure that the tax benefits which are provided with a view to enabling an industrial unit to modernise, are not frittered away elsewhere thus defeating their very purpose and allowing the industrial unit to be overtaken by obsolescence and resultant sickness. It is, therefore, highly desirable to ensure a linkage between modernisation and the benefits allowed for the purpose, by suitable legislative measures. To this end, the following measures are suggested :

- i) the total depreciation (including additional depreciation) must be provided for in the accounts.
- ii) a specified amount of such depreciation and of the amount of the Investment Allowance Reserve is invested in specific investments until needed for modernisation and
- iii) the amount thus invested to be used only for replacement of plant and machinery.

If the above suggestions are implemented, it should be ensured that :

- a) temporary tax gains arising from different methods for depreciation used for accounting and tax purposes are not dissipated,
- b) adequate amounts are available when necessary for replacement of assets and
- c) the tax benefits are

- i) charged to the accounts
- ii) separately invested and
- iii) provided for the required financial resources for replacement.

10.A.6 The aggregate allowance (both depreciation and investment allowance) available under the tax laws is still well below the cost of replacement of the assets, mainly because of the incidence of inflation. As the Committee has not had the benefit of any in-depth study of the impact of inflation accounting on the cost of replacement of the plant and machinery, etc. of an industrial unit vis-a-vis the allowances available under the tax laws for depreciation and investment allowance and due to the fact that introduction of inflation accounting for the purposes of taxation gives rise to many intricate problems, it is suggested that the issue of inflation accounting may be got studied separately by an appropriate authority having regard to the importance of the subject in the context of replacement, modernisation, etc.

10.B. MODERNISATION FUND

10.B.1. In this context, the Committee also considered the possibility of a Modernisation Fund at the national level. The amount of tax benefits indicated above could perhaps be invested in such a Modernisation Fund to be set up and administered as may be decided by the Central Government. Alternatively, the amount could be invested in bonds of the financial institutions which would in turn make the funds available at the time of modernisation. It may be added that based on the Central Budget of 1976, deposits aggregating Rs. 56.10 crores were made with the IDBI under the 'Companies Deposits (Surcharge on Income-tax) Scheme'. Likewise, the Central Budget for 1983 has made provision for similar deposits with the IDBI. Investment in bonds of the IDBI and other financial institutions providing funds for modernisation would, it is felt, be quite in consonance with the above objective. The details will have to be worked out in consultation with the Central Government and the financial institutions.

10.C. NATIONAL INDUSTRIAL REHABILITATION FUND

10.C.1 Any reconstruction (including restructuring of capital and liabilities) without equity support has no meaning. However, raising fresh equity for a sick industrial unit is rather difficult. In order to provide equity support to a sick industrial unit which is under the process of reconstruction under a package programme, interest-free funds are inevitably needed so that the sick industrial unit may achieve viability within a prescribed time schedule. The need has, therefore, long been felt for an 'Equity Support Fund'. Such a Fund which could also

help a sick industrial unit to overcome acute liquidity problems is required as a stand-by arrangement. In this context, the Committee has noted the existence of similar funds in certain foreign countries such as Italy, Germany, The United Kingdom and United States of America and feels that such a fund similar to the Long Term Operations Fund with the RBI could be created for providing equity support to sick industrial units. The Committee, therefore, recommends that a fund to be known as the 'National Industrial Rehabilitation Fund' may be set up for providing equity support to sick industrial units and such a fund would necessarily have to be in the nature of a fund of the last resort.

10.C.2 The assistance from the Fund may be made available either by way of a one time subsidy or equity participation, interest-free loans, interest subsidy to meet a part of the minimum chargeable interest for a specified period of time, or to compensate the banks and financial institutions for loss of funds resulting on account of rehabilitation schemes.

10.C.3 The Fund could be under the operational control of the IRCI, the Nodal agency of the Board for Industrial Revival.

10.D. REDUNDANCY FUND

10.D.1 Packages of rehabilitation may involve rationalisation of the labour force involving at times reduction in the labour force. Implementation of this part of the package may be hampered due to shortage of funds for compensating labour in a sick industrial unit in respect of voluntary retirement/re-trenchment. It is, therefore, desirable to have a Fund which could provide assistance towards redundancy payments. Similar Funds already exist in several countries like The United Kingdom and United States of America. A precaution must, however, be taken to ensure that the quantum of surplus labour in a sick industrial unit, if any, must be determined equitably. The assessment of labour requirement in a sick industrial unit must be impartially done. With this background, the Committee recommends the setting up of a Redundancy Fund.

10.D.2. The resources for both the above Funds could be raised either from tax benefits or from cess on the users of credit. It could also be strengthened by contribution from labour. A part of the retained profits of industrial units could also be contributed to the Funds. There may also be contributions to the Funds from the Central and State Governments.

10.E. WORKING GROUP CONCEPT

10.E.1 At present the rehabilitation programmes for sick industrial units are prepared by various agencies including private consultants and submitted to the banks and financial institutions. Based on a decision taken by the Standing Coordination Committee set up by the RBI, cases for making viability studies and rehabilitation schemes in respect of units where term lending institutions are involved, are referred to the IDBI and in other cases to the IRCI as per the decision of the Government of India, dated 19th November 1981. The rehabilitation schemes are discussed at inter-institutional meetings presided over by the IDBI or the lead institution or the lead bank as the case may be.

10.E.2 The schemes for rehabilitation of sick industrial units require effective coordination amongst the various banks and financial institutions involved, Central and State Governments as the case may be, management of the sick industrial units, labour and creditors, etc. In fact, as experience has shown, lack of co-ordination amongst the several agencies and apathy towards understanding and appreciating the problems of one another and the resultant delays have often created bottlenecks in the rehabilitation schemes which more often than not have been frustrated. The situation becomes more acute when one or some of the agencies have proceeded with implementation of their part of the scheme while others have been dragging their feet. Instances are so numerous that the matter calls for urgent and institutionalised handling.

10.E.3. To begin with, there should be a perfect understanding amongst all the participating agencies who are responsible for implementing the rehabilitation scheme. Experience shows that a long time is usually taken to agree to the relief measures or other steps required to be taken for rehabilitation; often lengthy correspondence ensues between the banks and financial institutions even when the rehabilitation schemes are drawn after mutual discussions.

10.E.4. Very often, when there is unanimity in the approach of the banks and financial institutions, the agencies take a long time to confirm the grant of certain reliefs and concessions under the package, say, in the nature of sales tax loans/reliefs, concessional water and electricity tariffs, rescheduling of Provident Fund and Employees' State Insurance dues, etc.

10.E.5 Insofar as legal constraints are concerned, these arise mostly due to the cumbersome and time-consuming procedures whether the question is of taking over the management of the concern by the Central

Government under the I (D & R) Act in terms of sections 18A to 18FH, or amalgamation or merger proposal in terms of the provisions of sections 391 to 395 of the Companies Act, 1956. There are sometimes legal difficulties in complying with the requirements of the Urban Land Ceiling Act as also in transferring the assets of a sick industrial unit from one district to another district in the same State or from one State to another State in the interest of availability of various essential inputs.

10.E.6 A need is, therefore, felt to have an agency or a standing forum where representatives of Central/State Governments, banks, financial institutions, labour, promoters, quasi-government bodies like electricity boards, etc. could be brought together for deliberations on the package scheme in respect of each sick industrial unit. There can be no denying the fact that every day's delay in the implementation of a rehabilitation package results in losses which by and large have ultimately to be borne in reality by the banks and financial institutions at least initially. The problem, therefore, needs to be tackled, so to say, on a war-footing. Already a Working Group previously under the IDBI and presently under the Exim Bank in the field of export finance is functioning exceedingly well over the years. It is high time that a similar Working Group mechanism be introduced in the field of rehabilitation of sick industrial units.

10.E.7 A special feature of the Working Group mechanism has been that commitments made by the representatives of various agencies are honoured by the respective agencies. One of the complaints about the inter-institutional/bank meetings has been that such meetings are often attended by junior level officials who are unable to take decisions on the spot and make any firm commitments on behalf of the institutions/banks they represent. The result is that the meeting turns out only to be a mere ritual rather than a decision making process. It is, therefore, highly desirable that the Working Group the Committee has in view is so constituted and so represented, that decisions taken at the meetings are implemented without delay.

10.E.8. The Committee, therefore, suggests that the Working Group which may be a standing working group may be headed by an institution which has adequate expertise in reviving sick industrial units. The Working Group should have as its permanent members senior level officials of the rank of Deputy Governor from the RBI, chairmen of term lending institutions, the chairmen of IBA, SBI, 3 other nationalised banks, representatives from the Central and State Governments (from Industries and Finance Departments) and representatives from other quasi-government bodies and the chairmen of concerned financing banks if not already members of the Working Group. The concerned labour union leaders and promoters will participate in respect of the sick in-

dustrial units in which they are involved. The package scheme as approved by the Working Group should be binding on the respective agencies. No other concessions/reliefs which do not find a place in the approved package should be given by any of the agencies, without prior reference to the Working Group unless that falls within the guidelines to be framed by the Working Group.

10.F. ERRANT MANAGEMENT

10.F.1 A concomitant consideration before the Committee related to the action to be taken in cases where sickness of an industrial unit is caused as a result of omissions and commissions on the part of the errant management and where due co-operation of the management is not forthcoming for the rehabilitation effort. A point has been made that further credit could be judiciously denied for new ventures of such errant managements. The Committee has considered the issue at considerable length. Such a course may be very difficult to adopt in practice due to various factors and may not be ultimately in the interest of industrial development. The Committee, therefore, feels that there could be a system of exchange of information on the management of the assisted industrial unit amongst the banks as also the financial institutions, so that by mutual consultations fresh assistance if extended is on terms which could be such as would ensure proper checks and balances and effective discipline on the affairs of the industrial unit.

10.G. SHARING OF CASH LOSSES :

10.G.1. The question of financing cash losses while nursing sick industrial units has been a subject of discussion by the Inter-Institutional Group constituted by the RBI, the term lending institutions and commercial banks and also at the meeting of the SCC constituted by the RBI to secure ongoing co-ordination between banks and term lending institutions.

10.G.2. Depending upon the nature and size of the industrial unit, cash losses could be incurred by a unit —

- a) before it is considered as a sick unit;
- b) after the unit has been treated as sick but before a rehabilitation programme is finalised and
- c) during the initial stages of rehabilitation of a sick unit.

Even in respect of such a unit there could be two types of situations :

- a) where banks have assisted the unit and the term lending institutions are not already involved;
- b) where both banks and term lending institutions have assisted the unit.

10.G.3. The recommendation of the Inter-Institutional Group was that where both the banks and term lending institutions are involved in the financing of an industrial unit, having regard to the structure and functions of the respective institutions, the financing of cash losses as a holding operation, if potential viability is established, should be shared by the banks and term lending institutions in all cases, where they are already jointly involved, in the same ratio as has been suggested for term loans in general; however, in determining their relative shares, the lending institutions may ensure that the loans provided by them do not end up in paying interest dues of other lending institutions. Further, in case where both the bank and the term lending institution are financing an industrial unit and the bank has agreed to finance the cash losses on its own, it should do so by way of a loan repayable over a period. In such an event, the term lending institutions, which may be holding first charge on the fixed assets of the industrial unit should concede pari-passu charge in favour of the banks in respect of such loans. The schedule of repayment of term loans sanctioned by the banks for financing cash losses should be drawn up in consultation with the term lending institutions, keeping in view the future cash generation of the industrial unit. However, the aforesaid recommendations were not accepted by the RBI and the term lending institutions in toto and the subject continues to remain a matter for discussion at the subsequent meetings of the SCC to secure on-going co-ordination between the banks and term lending institutions. The point at issue has been that since financing of cash losses is not the function of the banks, the term lending institutions should come forward to finance such losses. The view point of the term lending institutions is that as the term lending institutions had already indicated their willingness to step in whenever they were required to come in to provide funds to acquire additional fixed assets to replenish working capital finance diverted for financing acquisition of fixed assets, banks should not expect term lending institutions to do retroactive financing by recouping cash losses or providing funds to meet existing pressing liabilities, as that would only mean passing on the problem of the banks to the term lending institutions and the former improving their position at the cost of the latter.

10.G.4 One of the basic objectives of institutionalisation of credit is to make it a supervised credit. Unfortunately and without intending any criticism, it is not possible to supervise bank credit the same way as it could be done a few years back, mainly because of the tremendous expansion that the banks have undertaken and which has not been adequately

matched by development of manpower resources. In the process, the borrowers have often been able to take advantage and finance their cash losses through depletion of bank security. The result is that, by the time the bank is aware or is in a position to take any corrective steps, it has already in effect financed the cash losses. At this stage, to argue which agency should finance cash losses is rather an anachronism, though it could be termed as refinancing by the term lending institutions to the extent possible. This does not, however, happen with regard to the security of the term lending institutions who finance the fixed assets. The case, however, is entirely different where sickness has been detected and brought to the notice of all the concerned agencies, where the cash losses from a particular point of time have been identified and the sharing pattern as discussed in this chapter, has been agreed upon.

10.G.5 Since the existence of the cash losses cannot be denied, the Committee considers it absolutely essential that the problem is resolved satisfactorily in the best interests of the assisted sick industrial unit, banks and financial institutions. However, certain basic problems with regard to the financing of cash losses, which come to the fore can be summed up as under :

- What constitutes cash losses?
- Whether the cash losses should be reckoned after taking into account interest charges on term loans and working capital finance so that the loans granted to the unit for meeting cash losses are not utilised to pay interest charges due to another institution?
- What should be the security and how should it be shared between the banks and financial institutions?
- How the schedule of repayment of the term loans granted for meeting cash losses should be determined?

10.G.6. It has generally been the experience that in cases of chronic sickness, large irregularities in the accounts with banks have arisen not only as a result of cash losses incurred by the sick industrial units but also by way of debits raised by the banks in respect of interest charges (including penal interest) on the working capital finance and even on term loans. As per the accounting definition of cash loss, it is the loss taken after interest but before charging depreciation. Accordingly, the practice so far has been to include interest charges in the cash losses. The Committee feels that a distinction between cash losses and interest charges is significant and necessary inasmuch as the very objective of the concept of the rehabilitation scheme is to give a chance to the sick industrial unit to start operations with a more or less balanced position.

The Committee, therefore, recommends that for the limited purpose of sharing, the interest element should be excluded from cash losses. The amount of loss thus arrived at i.e. before interest and before depreciation may be termed as the 'Adjusted Cash Loss'. For the purpose of sharing, the figure of adjusted cash loss may be taken into account. In the case of a rehabilitation programme the interest should be allowed to be funded by the banks and the term lending institutions on a pro rata basis.

10.G.7. The Committee also suggests that where both the banks and term lending institutions are involved, adjusted cash losses may be met by the banks for the first year of operations following the implementation of the rehabilitation package. After that if any cash losses are envisaged or eventually emerge, the same for a maximum period of three years shall be borne by the banks and the term lending institutions on an agreed basis.

10.G.8. Interest on working capital finance should be segregated and has to be funded depending upon the circumstances and merits of each case. The funded interest may carry such rate as is agreed upon amongst the banks and the financial institutions based on the cash flow.

10.G.9. In so far as the schedule of repayment of term loans granted by the banks for meeting adjusted cash losses is concerned, the Committee suggests that the same should be determined by mutual consultation amongst the banks and the term lending institutions based on the cash flow. If in any particular year, cash generation is not adequate to meet the predetermined term loan obligations, both banks and term lending institutions in the first instance should insist on the borrower bringing in funds to meet not only the repayment obligations but also to maintain the required liquidity. However, where the borrower is unable to infuse funds, the banks and the term lending institutions should have a dialogue to review the position and upon satisfying themselves of the disability involved in the case, they might consider postponement of recovery of instalments and funding of interest, including interest on working capital advances from banks, on a pro rata basis.

10.G.10. It would be necessary, however, to ensure that the loss is not artificially inflated and that it reflects the true picture of the working of the sick industrial unit with reasonable expenses charged against its income. Such an exercise would be necessary when a decision to rehabilitate the chosen viable unit is taken in order to ensure that the assistance goes to genuine sick industrial units.

10.G.11. In so far as security is concerned, on finances provided by the banks for meeting the adjusted cash losses, a pari passu charge on the fixed assets of the concern may be provided to the banks for the funded

portion of the working capital and term loan advances. In other cases, the security pattern has to be evolved by the banks and the term lending institutions on a case to case basis by mutual consensus.

10.H AUDIT COMMITTEES

10.H.1. In order to combat sickness in the corporate sector the Committee has considered the feasibility of setting up 'Audit Committees' for each industrial unit.

10.H.2 The Canadian Institute of Chartered Accountants in its "Terminology for Accountants" has defined Audit Committees, in the following terms :

"Audit Committee — A Committee of Directors of a Corporation whose specific responsibility is to review the annual financial statements before submission to the Board of Directors. The **Audit Committees** Committee generally acts as liaison between the auditors and Board of Directors and its activity may include the review of nomination of the auditors, overall scope of the audit, results of the audit, internal financial control and financial control and financial information for publication".

10.H.3. Concept of Audit Committee is of recent origin and is not mandatory except in two or three countries. In other words, it is more or less recommendatory. The concept owes its origin not to the statute but to the need based concept of the progressive management, to fulfil the requirements and expectations of the investing public and shareholders at large. Inviting self criticism as a means of improvement of performance is also a new experiment. The Committee feels that in India too, Audit Committees could be constituted on a purely voluntary basis as an experimental measure for a duration of one or two years and their working be reviewed at periodical intervals and thereafter appropriate legislation be introduced if necessary, to give it a permanent footing.

10.H.4. The most purposeful advantage that can be achieved through the formation of Audit Committees is that such Committees may provide a fresh outlook to the overall problem of management. They would also provide relevant information to the outside directors quite effectively, who can thus keep an indirect control over the activities of the industrial units.

10.H.5 One or two non-official directors who are not saddled with the day to day operational responsibilities are nominated on the Audit committees to watch the beep signals at the incipient stage of sickness itself.

10.H.6. The statutory auditors should report periodically their findings to the Audit Committees about the important and critical matters of the industrial unit. Audit Committees can thus serve as an important mode for establishing rapport between the Board of Directors of the industrial unit and its statutory auditors.

10.I INTEREST SUSPENSE ACCOUNT

10.I.1. The banks and financial institutions generally maintain their accounts on a mercantile basis, that is to say, income and expenditure are recorded on the basis of their accruals rather than on cash basis. Where the accounts are kept on a mercantile basis, interest on doubtful debts is taxable irrespective of whether the interest is actually received or not since the interest amounts have been entered in the books of accounts of the banks and financial institutions and treated as income for all practical purposes. This causes undue hardship to the banks and financial institutions. While on the one hand the amount of interest is not actually recovered by them from the sick industrial units, on the other since such interest amount is taken into account, they pay income tax on this income which is doubtful of recovery. This causes considerable hesitancy on the part of the banks and financial institutions to agree to reliefs in respect of interest when packages are framed. The Committee recommends that interest charged by the banks and financial institutions on advances made to sick industrial units should not be taxed till the same has actually been recovered. A suitable amendment may be made in the Income Tax Act for this purpose and necessary guidelines may be framed therefor.

10.J. INTEREST TAX

10.J.1 Interest tax is being levied on the banks and financial institutions on their interest income. The incidence of this tax is allowed to be passed on by the banks and financial institutions to all the borrowers including sick industrial units. While formulating packages of rehabilitation of sick industrial units the banks and financial institutions are normally granting various concessions by way of reduction in rates of interest, waiver of penal interest, funding of interest, reduction in margins, rescheduling repayments of loan instalments, etc. Thus, while on the one hand the banks and financial institutions agree to reduce the rates of interest on their advances to sick industrial units as per the rehabilitation package, on the other the full impact of such reduction is not felt by the sick industrial units as the rates of interest charged include the component of interest tax. Apparently this seems to go against the spirit of giving reliefs under the rehabilitation package.

10.J.2 In this context the Committee felt that in view of the various reliefs required by a sick industrial unit to turn the corner and also the interest evinced by the Government in the rehabilitation of sick industrial units, it would be desirable if the advances given to sick industrial units are exempted from interest tax, at least during the period till the concessions are discontinued by the banks and financial institutions. Although the interest tax has been reduced from one percent to half percent in the 1983-84 Central Budget, the Committee suggests that exemptions from payment of interest tax in the case of sick industrial units will be more appropriate.

10.K PROTECTION TO NOMINEE DIRECTORS

10.K.1. As a matter of general policy banks do not encourage appointment of their officers on the Board of Directors of industrial units assisted by them. However, the banks with their large financial stakes in industrial units, can no longer afford to remain aloof. The banks have, therefore, to seriously consider appointing their nominees on the Board of Directors of such assisted industrial units. In this area, however, banks face major problems. A bank's nominee director, as any other director of the industrial unit is subject to the same obligations and liabilities as any director of the industrial unit. Unlike the nominee directors of the financial institutions such as the IFCI, IDBI and SFCs, the nominee directors of the banks do not have statutory protection from prosecution in case of default of the industrial units. This is the major deterrent factor for the successful implementation of the policy for appointing nominee directors representing banks in assisted units. The Committee felt that it is desirable that the banks should have the right to appoint nominee directors who are statutorily recognised and to provide for statutory protection for them. Protection to such directors nominated by the banks cannot be given unless a statutory provision is made in that behalf in the relevant statute on the lines of Section 38(a) and 25(3) (b) of the IFCI Act, 1948.

10.L INDUSTRIAL MANAGEMENT POOL

10.L.1. One of the major causes of sickness, as indicated earlier in the Report, has been management deficiency. At the same time, capable and dedicated managers to man the various positions of responsibility in the sick industrial units are difficult to find in desired number and more difficult to attract especially when they have to face the multi-dimensional problems of sick industrial units.

10.L.2. The basic problem of management vis-a-vis programme of industrial development was well recognised in the Industrial Policy Resolution, 1956 :

“This programme of industrial development will make larger demands on the country's resources of technical and managerial personnel. To meet this rapidly growing need for the operation of the public sector and for the development of the village and small scale industries, proper managerial and technical cadres in the public services are being established.”

10.L.3. In adherence to the above policy, industrial services both at the Centre and in the various States were geared up mainly for promotional work. Government of India also established an Industrial Management Pool by selecting technical and managerial personnel from private sector industries and trade, mainly to man the public sector trading and manufacturing organisations. Although the cadre continues even today, direct recruitment to the Industrial Management Pool was discontinued after a year of its creation. The executives selected to the Pool have proved enormously successful in managing even large public sector undertakings.

10.L.4. In November 1976, the RBI advised the banks that in many cases remedial action required to be taken by the banks would not be confined only to financial controls but also extend to improving/changing the borrowers' management and removing deficiencies of various types in the rearrangements for purchase, production, marketing, etc.

10.L.5. The Working Group on the problems of sick units, constituted following the Prime Minister's meeting with the Chief Executives of banks and financial institutions in October 1978, states : “the difficulties experienced by the banks and the term lending institutions in locating suitable qualified persons to assist in the management of sick units were noted. It was considered necessary that term lending institutions should be constantly on the look out for qualified persons and while maintenance of panels may be of help, it may not be a complete answer. Efforts should also be made to maintain liaison with the public sector undertakings so that the services of experts and technicians working in these undertakings could be borrowed for specified periods in the task of rehabilitation of sick units. It was noted that the IRCI was already doing this to some extent and that it has already established a Management Pool.”

10.L.6. The policy guidelines for sick industries issued by the Government of India in October 1981 observe, inter alia, that the financial institutions would be required to assume management responsibility and in this context, the institutions particularly the IDBI should consider the

feasibility of creating a cadre of professional managers who may be entrusted with the management of the units in which financial institutions have made substantial investments.

10.L.7. A Committee constituted by the Inter-Institutional Meeting of the financial institutions, in January 1982, considered the aspect of creating a management cadre. It observed that assumption of management responsibility by the banks and financial institutions was fraught with various risks, both legal and pecuniary and might also conflict with corporate objectives of the institutions. However, takeover of management could be resorted to as a temporary expedient in cases where sickness was primarily due to management deficiency but the sick industrial unit was found to be potentially viable and the institutions had substantial stake in the project. The Committee observed that the proposal of creation of a special cadre of professionals was a step in the right direction and early formation of such a cadre would be of considerable help to the institutions in assuming management responsibility even for a limited period.

10.L.8. The need for maintaining a Data Bank of executive personnel who may be drafted at short notice for managing the affairs of sick industrial units in various functional areas cannot be overemphasised, since time is of essence in tackling the problems of sick industrial units. It is, therefore, essential that a pool of executives in different disciplines, viz. technical, legal, financial, commercial and administrative is maintained where persons of the required discipline and calibre are available, so to say, at call.

10.L.9. While the need for such a pool has been fully recognised by the Central Government, the banks and financial institutions, the modalities of its maintenance and updating involve laborious and expensive process. The banks and financial institutions have been chary to keep such management personnel on their regular rolls. Also, it may not always be possible to offer appointments to the selected persons on an immediate basis. Another important question has been the payment of remuneration during the idle time if the personnel are not in position in a sick industrial unit. The idea of a separate subsidiary of institutions had been mooted, whose job it would be to keep such personnel on their regular rolls and draft them as and when required. Such a subsidiary could be funded by the banks and financial institutions by contribution to its share capital, subscribing to its bonds, etc. No concrete steps, however, have so far been taken in this regard.

10.L.10. An alternative could be that the persons who are engaged in different industries, both in the public and private sectors, may be empanelled with the consent of their employers and in times of need, they could be drafted on the job at short notice.

10.L.11. The only institution which has created a pool of managers is the IRCI. The pool was found effective on two major counts. On the one hand, the executives reluctant to serve on the roll of sick units which were in general financially weak, find job security on the rolls of the IRCI and on the other, successful executives have the chance of facing the challenges and mobility to larger units with scope of promotion to higher grades. Initially, capable and experienced persons were, therefore, attracted to the IRCI. But gradually the task appeared to be more difficult and over time quite some Pool Officers have shown a tendency to seek better jobs outside. The pool keeps on thinning and needs frequent replenishment.

10.L.12. The system of maintaining an Industrial Management Pool, as such, is not free from anomalies. One of the difficulties to maintain the panel and exploit it advantageously is that with reference to the specific requirements of the sick industrial units or to fill up vacancies in a particular field of specialisation, right type of candidates may not be readily available. Secondly, the chief executives appointed for a sick industrial unit may not find a harmonious team of second tier officers and often need change to revamp the functional areas. At times, empanelled candidates who are not offered any assignment for a long time may lose interest. Thirdly, a person empanelled with the Pool and deputed to an assisted sick industrial unit may be temporarily out of employment. He would then look to the Pool for payment of his salary which the Pool Management may not be in a position to reimburse as normally the salaries and perquisites are borne by the units themselves directly. Fourthly, such Pool officers in the sick industrial units may not possess a sense of belonging to that unit which would otherwise have been there if the sick industrial unit had recruited the incumbent directly. Such executives sometimes because of their attachment to the Pool may be the victims of dual accountability, one to the sick industrial unit and the other to the Pool, which is not desirable. All the same, the advantages of maintaining the Management Pool cannot be exaggerated. More so, this would save much loss of time to follow the dilatory and expensive process of recruitment in each individual case. The Committee, therefore, recommends that the Industrial Management Pool maintained in the IRCI be broad based and strengthened with sufficient number of persons of various disciplines, functional areas and grades, industry-wise, so that the banks and financial institutions may also draw upon them if needed for quick postings in their assisted sick industrial units.

10.L.13. Central Government may also consider the creation of an Industrial Management Service on the lines of the Indian Administrative Service, Indian Police Service, etc. It may incidentally be mentioned that in some of the States like Karnataka, Maharashtra, Orissa, etc.

officers belonging to the Indian Administrative Service have been posted in responsible positions in industrial units and their performance is reported to be by and large satisfactory.

10.M. DETERMINING THE RESERVE PRICE FOR THE SALE OF AN INDUSTRIAL UNDERTAKING

10.M.1. Occasions do arise when the banks and financial institutions decide to put an assisted industrial unit on sale with a view to recover their dues or for the purpose of reconstruction by induction of new management in the process. While **Reserve Price** this may be effected by various methods such as auction, direct sale, sale through court, etc. it would be necessary to fix a basic price below which the sale would not be effected. Reserve price is also required to be fixed for disposal of units taken over under the I (D & R) Act. The problem being thus of importance and vital as much to the needs of rehabilitation of sick industrial units as to recovery of the dues of the banks and financial institutions, the Committee obtained the opinion of Shri Y. H. Malegam, a reputed Chartered Accountant. A copy of the note submitted by him is given in Appendix-IV. The Committee also had the benefit of a Sub-Committee headed by Shri Y. V. Sivaramakrishnayya, Chairman & Managing Director of the Bank of Baroda, which further examined the issue. The sale of a sick industrial unit may be either on 'running concern' basis or on 'liquidation' basis. To decide either of the alternatives, it has to be seen whether the sick industrial unit can make an operating profit before paying interest; if so, the unit can be sold as a running concern. If no profit can be made as such, an attempt should be made to see whether fresh investment can induce such profit. If the result is negative even after this, the sale can only be on the basis of liquidation value.

10.M.2. When sale is made on the basis of liquidation, the assets may not be disposed of as an integrated unit. Further, such sale presupposes that these assets need not be used for the purposes for which they were acquired by the concern. Obligations such as continuation of the services of employees, etc. are not normally carried along with such sale. However, if any encumbrances or obligations are passed on to the purchaser or if there are any restrictions on the free use of the assets, suitable discounts have to be given while fixing the reserve price. Similarly, allowance has to be given for changes in technology, etc. concerning the unit.

10.M.3. Where a unit is proposed to be sold as a running concern, there are several factors to be considered as follows :

- a) Surplus land and valuable tenancies, the value of which is to be taken at the full market value;

- b) Investments which are also to be valued at the quoted prices;
- c) The locational advantages and infrastructural facilities readily available for the unit and other factors like reduction in the gestation period for commencement of production in a new unit of similar nature can also be monetised;
- d) Other assets or positive factors like industrial licences, import or indigenous quotas, etc. can also be exploited by assigning appropriate values;
- e) Similarly, where the unit's products have established a name in the market, the element of such goodwill should also be included in the valuation;
- f) The extent of tax benefits available to the purchaser on account of the accumulated losses of the unit also need to be included in the valuation.

10.M.4. Fixed assets can be valued in terms of their operating capability. In so far as current assets are concerned, finished goods can be valued at the realisable value less estimated expenses for sales, holding charges, etc.; work-in-progress can be valued at the realisable value of finished goods which can be produced out of the same less cost of such conversion and estimated expenses for sales and holding charges, etc. of such finished goods; raw materials can be valued at replacement cost. While valuing book-debts, allowance has to be given for non-realisable debts.

10.M.5. While giving allowances, the extent of encumbrances or obligations which will be passed on to the purchaser need to be kept in view. Similarly, liabilities on account of staff, viz. liability for the accumulated benefits being taken over, retrenchment compensation payable if any and the burden of surplus staff if no retrenchment is possible, should also be kept in view.

10.M.6. Though several intangible factors mentioned above are to be included in valuation, it may be pointed out that monetising too much of these intangible advantages will not leave it worthwhile to induce the potential purchaser. At the same time, with large investments of public funds in such units, they cannot be sold for trifling amounts. Therefore, apart from fixing a specific amount as a reserve price it may be advantageous to indicate a flexible range within which the sale price could be negotiated.

10.M.7. The reserve price arrived at on the basis of suggestions given above may not always be feasible as the intending purchaser would not have adequate incentives to submit bids, particularly where the yield

on 'owned funds' of other units in the same industry are higher. In such cases, the return of 15 per cent (interest rate on term loans) assumed on 'owned funds' will need to be increased suitably.

10.M.8. The reserve price for cash down payment and payment in instalments should be different. The reserve price for cash down payment could be the value arrived at as per the formula. On the other hand, if the purchase consideration is to be paid in instalments free of interest or at a concessional interest, the reserve price will need to be raised suitably.

10.N. STAND-BY INSTITUTIONAL ARRANGEMENTS

10.N.1. The Committee in terms of item (vi) of its memorandum dated 14th May 1981, is required to suggest stand-by institutional arrangements (other than nationalisation) for purchase of undertakings or shares in companies owning the undertakings, in the absence of private purchasers or in competition with them, in the case of viable units so as to protect to the maximum extent possible, the institutional funds already involved in the undertakings.

Stand-by institutional arrangements for purchase of undertakings

10.N.2. Where the causes of sickness of an industrial unit could be traced to its existing ownership, and a change of ownership/management is considered as one of the measures for its rehabilitation, occasions may arise when buyers may not be forthcoming at the appropriate time to take over the sick industrial units as a result of which the banks and financial institutions involved may be faced with the prospect of disposal of the sick industrial unit at an uneconomic price which will not be advisable.

10.N.3. Nationalisation would, of course, result in physical reconstruction of the sick industrial units but not necessarily their rehabilitation. It is also realised that nationalisation is not a panacea in all cases except perhaps when 'public interest' is involved.

10.N.4. In such a situation what is needed is a stand-by institutional arrangement, whereby the sick industrial unit could be taken over by an institution as part of its designated functions, if so directed by the Central Government, without having to hunt around for buyers, the underlying intention being that such institution will acquire the sick industrial unit not only to negotiate for a fair price but also, where considered necessary nurse it back to health, whereafter it could be disposed of for a fair commercial consideration.

10.N.5. One of the modes of acquiring a sick industrial unit is by obtaining majority of its equity shareholdings. The advantage in such acquisition is that it saves the expenses of incorporating a new company and also without the necessity of purchasing the entire equity share capital of the sick industrial unit; in other words, acquiring shareholding over 50% can be held to be sufficient; moreover this eliminates the need to obtain a similar footing in the preference share capital or debentures issued by such sick industrial unit. Such a system of acquisition is prevalent in other countries also. For example in Italy, GEPI, s.p.a. (Industrial Participation and Management Society) a shareholding firm controlled by CIPI is performing this function. GEPI receives a request from the firm in crisis, after assessing its viability, the sick firm is taken over in partnership with the private partner. Only rarely does it intervene, if a private partner is not found. The firm is then nursed back to health, after which GEPI as provided by law must come out of the management, which passes entirely to the party. Other companies are sold as soon as they are reorganised completely. The National Enterprise Board in the U.K. set up on 20th November 1975 as a statutory public corporation under the Industry Act, 1975, acts as a holding company for shareholdings in industrial companies which it has acquired either through its financing activities (NEB's finance is normally provided in the form of equity) or through the transfer of shareholdings to it by the Government (e.g. British Leyland Ltd., Rolls Royce Ltd.). The NEB, in its operations enjoys no special privileges over the private sector, by reason of its publicly owned status.

10.N.6. Having regard to the role of the IRCI in revival of sick industrial units, the Committee is of the view that it would seem appropriate that the IRCI would be the proper body for carrying on the above function of providing a stand-by institutional arrangement for takeover of sick industrial units. However, as the other all-India term lending institutions (like the IDBI, IFCI and ICICI) are also undertaking rehabilitation of sick industrial units and in terms of the guidelines issued by the RBI to banks to refer cases of sick industrial units for rehabilitation where the term-lending institutions are involved to the IDBI, the Committee considers it desirable that the other all-India term lending institutions should also be vested with powers to purchase, obtain on lease or otherwise acquire and sell, lease out, transfer or otherwise dispose of any industrial or business undertaking so that they may also function as stand-by institutions for acquiring sick industrial units. The Committee further suggests that the stand-by institutional arrangements may be better implemented under a consortium arrangement amongst the IDBI, ICICI and IFCI. In performing the above function, the IRCI, which was created as a specialised body to undertake reconstruction work which was ordinarily outside the scope of operations of the banks and financial institutions, would be fulfilling its role in this

regard. As a safeguard, guidelines may be framed for carefully identifying the sick industrial units and the modalities for acquiring and disposing thereof.

10.O. RECOMPENSING AFTER REVIVAL

10.O.1 The packages of reliefs and concessions being extended by the banks and financial institutions have been discussed in Chapter-IV. The issue whether the institutions should reserve for themselves the right of getting themselves properly recompensed for any past concessions granted by them in the event of the sick industrial units attaining normal health and sound financial position, was considered by the Committee both from the economic and legal aspects.

10.O.2 The economic justification for a proposal for recompense is high, since the banks and financial institutions operate inter alia on funds which have a cost factor. Legally also in consideration of having granted the concessions, it is possible for the banks and financial institutions to have the right reserved for getting themselves recompensed for any concessions granted by them after the sick industrial units have been rehabilitated. This expedient would normally be justifiable, where there is no change in the controlling interest/management or the new entrepreneur/management being inducted is agreeable to that sort of an understanding and is prepared to bind himself to such an undertaking. Difficulties would, however, arise where the revival is through amalgamation or merger under the provisions of the Companies Act, Income-tax Act (vide section 72A), etc. Where the amalgamation/merger proposal is being considered by a High Court, the stipulation on the part of the banks and financial institutions reserving for themselves the right of recompensation might not be acceptable to the High Court approving the schemes of merger on the basis of certain declared and specific sacrifices, unless the recompense forms a part of the scheme itself.

10.O.3 The Committee is fully conscious of the degree of discrimination underlying such a differential treatment, but having regard to the consideration that the same control and ownership with or without identity of management is being continued which reaps the benefit of revival, which in turn is at least partially dependent upon the sacrifices agreed to be made, the Committee would, on balance, suggest that a sick industrial unit, where no change in the management/controlling interest or amalgamation or merger is involved, the stipulation regarding recompense could be made while granting the reliefs and concessions and once these are accepted by the assisted unit, it would be binding on the concerned parties and can be enforced by the banks and financial institutions at the appropriate time after the sick industrial unit has been rehabilitated.

10.O.4 The Committee observed that under the German Law, where a borrower can pay upto 35% of the debt within a year or 40% beyond a year, he can apply to the court for compromise and when approved, the borrower's debts are settled accordingly. In the case of bankruptcy, however, a creditor has a right to recover the unsatisfied claim upto a period of 30 years.

10.O.5 The Committee feels that there seems to be every justification that institutions should give the concessions and reliefs only till such time that the sick industrial units come to a healthy stage. Once the sickness and the period of convalescence is over and such units have attained their normal health, units should be subjected to the same rigours and discipline as are applicable to other normal units in the same situation. In this view, it would seem desirable that while granting reliefs and concessions, a stipulation is made that the banks and financial institutions should have a right to review the rate of interest prospectively and retrospectively or to have accelerated repayment of the principal amount if the financial position of the units permits. They could also, as a recompense, ask for restitution wholly or partly of the sacrifices made by way of write offs or conversion of dues into equity. In either case, the extent of the right should be predetermined.

10.O.6. One way of keeping the agreed recoverable dues is the issue of 'below the line' debentures as a contingent liability, particularly in view of the various problems to be faced before the Income-Tax authorities in reopening the cases where certain basis was followed by the banks and financing institutions to claim the tax relief. The debentures will, of course, be unsecured debentures which the company should purchase in the event of cash surplus for cancellation in varying lots. Guidelines in this regard would have to be worked out in consultation with the Controller of Capital Issues.

10.P SECTORAL STUDIES

10.P.1 Industry-wise or sector-wise sickness calls for a macro level approach both in the matter of diagnosis as also treatment. The Committee feels it necessary that sectoral studies of particular types of industries where there is concentration of sickness should be undertaken either by specified institutions or by constituting ad hoc task force and wide representation. Such studies should be a constant feature and the report should be submitted to the concerned Ministry/Department for taking appropriate action. Copies of such reports should also be made available to the secretariat of the Working Group referred to in paragraph. 10.E.6.

10.Q. AGRO-BASED INDUSTRIES

10.Q.1. In the case of agro-based industries, beset with problems peculiar to such type of industries, the assistance of the National Bank for Agriculture and Rural Development and banks may be taken in the preparation of such sectoral studies.

10.R. ROLE OF THE IRCI PENDING CREATION OF THE BIR.

10.R.1. It was brought to the notice of the Committee that the proposal to convert the IRCI into a statutory corporation is in an advanced stage and that the powers as vested in the SFCs and IFCI are being vested in favour of the IRCI. Further, the IRCI may also have powers with suitable modifications with regard to the sale and reconstruction of industrial units as per the provisions in the I (D & R) Act and those relating to mergers. The Committee, therefore, recommends that within its scope, the IRCI may deal with cases of rehabilitating sick industrial units referred to it by the banks and financial institutions during the interregnum pending creation of the BIR referred to in Chapter-VII.



CHAPTER XI

SUMMARY OF RECOMMENDATIONS

- 11.1 Timely detection of symptoms of sickness and formulation of a nursing programme is an essential requisite at the incipient stage itself. No rigid definition of incipient sickness can be laid down and some element of flexibility should be left to the judgement of the institutions. In consortium or multi-agency finance, there should be periodical exchange of information on the unit between the different agencies. A common format for obtaining such information from the unit by the concerned institutions be evolved. If any institution desires to call for additional information, it may do so and share the same with others if it throws alarm signals (paragraph 4.14).
- 11.2 To have a purposeful monitoring system of the sick industrial units financed by them, banks may have their present set-up studied by institutions like the National Institute for Bank Management, for appropriate strengthening of the same (paragraph 4.24).
- 11.3 Viability on a commercial basis should be the main criterion for undertaking rehabilitation of a sick industrial unit. If rehabilitation is taken up on considerations other than commercial viability, the monetary sacrifices made by the banks and financial institutions should be well protected (paragraphs 4.16 and 5.9)
- 11.4 Definition of viability of a sick industrial unit is :
"A unit may be regarded as viable if it would be in a position, after implementing a package of concessions, spread over a period not exceeding seven years from the commencement of the package, from banks, financial institutions, shareholders, labour, suppliers of goods and services or other creditors, as may be necessary, to continue to service its repayment obligations as agreed upon, including those forming part of the package, without the help of the concessions after the aforesaid period. The repayment period for restructured debts should not exceed ten years from the date of the implementation of the package and such a unit should be in a position to commence, if possible, declaration of dividend, both preference as well as equity, within a period of seven years" (paragraph 5.10).

11.5 Package of rehabilitation of a sick industrial unit may be based on :

- i) financial implications based on the possible sacrifices from all the concerned agencies;
- ii) the merits of the case in such a manner that a viable (as defined in paragraph 11.4 above) sick industrial unit will be rehabilitated to normal health at the earliest, in not more than 7 years from the start of the implementation of the package of rehabilitation while keeping the total sacrifices to the minimum;
- iii) conversion of term loan into equity capital, reduction of equity capital, postponement of overdue interest, conversion of overdue interest into term loan and reduction in the concessional rates of interest wherever necessary; the types of concessions and the extent thereof may be considered on the merits of each case;
- iv) within the time frame of seven years for rehabilitation of a sick industrial unit, dividend may be distributed once it comes out of the red and before all institutional long term dues are fully discharged and as and when warranted depending on the merits of the case, concessions extended may be reduced or withdrawn (paragraph 5.11).

11.6 The remedies as available in terms of various existing statutes for reviving and rehabilitating sick industrial units are inadequate and dilatory. Making amendments to the existing laws may not achieve the desired objective because it would require a large number of amendments, substantial as well as consequential. Having regard, therefore, to the existing legal framework vis-a-vis rehabilitation of sick industrial units, a comprehensive special legislation designed to deal with the problems of sick units is necessary (paragraphs 6.1 and 6.2).

11.7 Definition of a sick industrial undertaking for the purpose of the Special Legislation is :

“A sick industrial undertaking is an industrial undertaking which expression also includes a Company or Co-operative Society owning the industrial undertaking, as the case may be, and which has all the following characteristics and also those as have been taken over and continue to be so taken over under the Industries (Development & Regulation) Act, 1951, namely :-

- i) the industrial undertaking incurs in the immediate preceding accounting year cash loss as disclosed in the audited or the proforma balance sheet that is to say the loss arrived at in

the manufacturing/profit and loss account of such industrial undertaking after making provisions for all expenses, including interest as also accrued interest but without providing for any depreciation (in accordance with the provisions of the Companies Act, 1956) and transfers to reserves like Development Rebate Reserve, Investment Allowance Reserve, General Reserve, etc.;

- ii) the current ratio that is to say the ratio between current assets and current liabilities as disclosed in the audited or proforma accounts of the immediate preceding accounting year of such industrial undertaking proves adverse according to the prevalent commercial accounting practice; and
- iii) the accumulated losses of such industrial undertaking as at the end of the immediate preceding accounting year result in erosion of 50% or more of its net worth or in any erosion of its paid up capital (Paragraph 6.4)."

11.8 A quasi-judicial body called the Board for Industrial Revival may be set up under the special legislation to deal expeditiously and exclusively with matters relating to rehabilitation of sick industrial units. The Board will have the powers of a Civil Court in passing orders and in matters of enforcement thereof. To ensure finality and speed, the decision of the Board should be made non-justiciable, except the writ and other jurisdiction of the High Courts and the Supreme Court (Paragraphs 7.1 and 7.4)

11.9 Special tribunals to serve as quasi-judicial bodies to deal exclusively with the recovery of dues of the banks and financial institutions by following summary procedures may be created (Paragraph 8.3 (vi)).

11.10 For creating a security in favour of the banks and financial institutions over land, the Urban Land Ceiling Legislation may be amended suitably (Paragraph 8.3 (vii)).

11.11 A special procedure in the legislation for creation of statutory charge in favour of the banks and financial institutions should be made (Paragraph 8.3 (viii)).

11.12 It is necessary to ensure that the obligations of the banks and financial institutions for sharing the distributable proceeds are adequately tied up through agreements/arrangements (Paragraph 8.3 (xiv)).

- 11.13 Recommendation of the Banking Laws Committee regarding creation of mortgage by deposit of title deeds and registration of charges created by way of hypothecation of movables may be pursued by the RBI with the Central Government (Paragraph 8.3).
- 11.14.1 Apart from monetary concessions from banks and financial institutions, other agencies, such as the Central/State Governments, management, labour, shareholders, depositors, creditors, etc., should also contribute their mite in the package of rehabilitation (Paragraph 9.2).
- 11.14.2 Concessions from the Central Government may be made applicable to sick industrial units as a class. These concessions envisaged are exemption from Central Excise, wholly or partly, for a period of time, exemption from interest tax and income-tax on interest suspense account in the case of banks in regard to sick industrial units, preferential allotment of canalised items to sick industrial units, deferment/rephasing of contribution to Provident Fund, Income Tax, Employees' State Insurance Fund, etc., deferment of payment of minimum bonus for a limited period, extending market support by reserving certain quota for purchase from sick industrial units, etc. (Paragraph 9.A.1).
- 11.14.3 State Governments may assist sick industrial undertakings in the form of ensuring preferential treatment in respect of power supply, concessions in power tariff for a specified period, exemption or concessions in the rate of sales tax/octroi duty, etc., speedier disposal of industrial disputes, adequate market support for the products by strengthening infrastructure, waiver of penal levies, declaration of sick industrial units as Relief Undertakings, price preference in the matter of purchase, grant of expeditious permission under the Urban Land Ceiling Act for purposes of mortgage/sale, etc. (Paragraph 9.B.)
- 11.14.4 Management should co-operate by foregoing interest on unsecured loans/deposits brought by self or friends and relatives, write-off of the loans and bringing in fresh funds as may be decided under the package (Paragraph 9.C.).
- 11.14.5 Labour may contribute by voluntarily agreeing to a scheme of rationalisation/retranchment, wage stabilisation, agreeing not to raise any fresh demand for an agreed period, increased productivity, productivity linked incentives, moderation of fringe facilities for a period of time, etc. (Paragraph 9.D.1).

- 11.14.6 Shareholders should voluntarily agree to any scheme of restructuring, resulting in writing down the value of shares, share exchange value in the case of merger or amalgamation, pledge or deposit of their shares with the financing agency and transfer of voting rights, etc. (Paragraph 9.F.).
- 11.14.7 The depositors and trade creditors may agree to a phased liquidation of past dues, desist from filing winding-up petitions, extend co-operation at creditors' meetings to any scheme of reconstruction, merger, etc. (Paragraphs 9.F. & G.).
- 11.15 So that the tax benefits provided with a view to enable an industrial unit to modernise are not frittered away elsewhere, a linkage between modernisation and the corresponding tax benefits allowed for the purpose should be ensured by suitable legislative measures (Paragraph 10.A.5).
- 11.16 In the context of replacement and modernisation of plant/machinery, etc. the issue of introduction of 'inflation accounting' for the purpose of making provision for depreciation and investment allowance under the tax laws may be got studied by an appropriate authority (Paragraph 10.A.6).
- 11.17 In the context of modernisation, setting up of a 'Modernisation Fund' at the national level may be considered (Paragraph 10.B.1).
- 11.18 Setting up of a 'National Industrial Rehabilitation Fund' to provide equity support/overcome liquidity problems of sick industrial units may be considered (Paragraph 10.C.1).
- 11.19 Setting up a 'Redundancy Fund' for compensating labour may be considered (Paragraph 10.D.1).
- 11.20 In order to avoid delay in arriving at a commonly committed package programme (of a sick industrial unit) amongst the participating agencies, an agency or a 'Standing Forum' (Working Group) may be constituted whose decision should be made binding on all the participants (Paragraph 10.E.8).
- 11.21 A system for exchange of information on the management of the assisted industrial units amongst the banks and financial institutions may be introduced (Paragraph 10.F.1).
- 11.22 'Adjusted cash loss' i.e. loss before interest and depreciation may be shared between the banks and financial institutions on certain indicated bases (Paragraphs 10.G.6 — 10.G.11).

- 11.23 Appointment of 'Audit Committees' may be considered to serve as an important mode for establishing rapport between the Board of Directors of the industrial unit which may include nominee directors of the banks and financial institutions and its statutory auditors (Paragraphs 10.H.3 — 10.H.6).
- 11.24 Income Tax Act may be suitably amended to exempt payment of tax by the banks and financial institutions on interest kept in Interest Suspense Account (Paragraph 10.I.1).
- 11.25 Advances to sick industrial units under rehabilitation programme of the banks/financial institutions may be exempted from the incidence of interest-tax (Paragraph 10.J.2).
- 11.26 Banks' and other financial institutions' nominee directors on the Boards of industrial units may get the necessary statutory protection (Paragraph 10.K.1).
- 11.27 An 'Industrial Management Pool' may be created and maintained by the financial institutions. Government may also create an 'Industrial Management Service' to man the industrial units on the lines of the Indian Administrative or Indian Police Service, etc. to man the industrial units (Paragraphs 10.L.12 — 10.L.13).
- 11.28 While effecting sale of an assisted industrial unit whether as a running concern or on liquidation basis it would be desirable to fix a 'Reserve Price'. The computation should also take into account non-physical factors like gestation period for a new unit, industrial and import licences and quotas, goodwill and tax benefits as and where available. Reserve price for payment in instalments should be higher than the cash down payment (Paragraphs 10.M.1 — 10.M.3 and 10.M.8).
- 11.29 A stand-by institutional arrangement may be made whereby the sick industrial units could be taken over as a stop-gap arrangement by an institution as part of its designated functions with a view to negotiating for a fair price for its ultimate sale (Paragraph 10.N.4).
- 11.30 The banks and financial institutions may, in appropriate cases, have a predetermined right to get themselves recompensed for the concessions given by them, if necessary through 'Below the Line Debenture' mechanism (Paragraph 10.O.5).
- 11.31 In order to grapple with the problems affecting particular type of industries where there is concentration of sickness, sectoral

studies may be undertaken by specified institutions or by constituting adhoc task force (Paragraph 10.P.1).

- 11.32 In respect of agro-based industries, assistance of the National Bank for Agriculture and Rural Development and the banks may be taken for sectoral studies (Paragraph 10.O.1).
- 11.33 During the interregnum, pending creation of the BIR the IRCI may deal within its scope with cases of rehabilitating sick industrial units referred to it by the banks and financial institutions (Paragraph 10.R.1).

T. Tiwari
Chairman

"in terms of my letter dated 28-9-1983"*

Dr. R. K. Hazari (Member)	Dr. P. D. Ojha (Member)
Y. V. Sivaramakrishnayya (Member)	D. N. Davar (Member)
D. R. Mehta (Member)	P. K. Ahuja (Member)
R. Jagannathan (Member)	S. C. Mittal (Member)
K. L. Roy (Member)	R. Viswanathan (Member)
C. Chandrasekhar (Member)	S. A. Naik (Member)
M. K. Chubby Raj (Member)	Kum. S. V. Maruthi (Member)

S. Jayaraman (Member-Secretary)

* Please see page 119.

R. K. Hazari
Tel. (022) 387043.
September 28, 1983.

8 Maheshwar N ketan
5 B Pedder Road
(Dr. G. De hmukh Marg)
Bombay-400 026.

Dear Shri Tiwari,

I have gone through the report of your committee and have great pleasure in appending my signature. Let me thank you and other members of the Secretariat again for the opportunities given to me as member of the committee and the consideration extended to me at all times.

While I am in agreement with the conclusions and recommendations in the report, I have some reservations regarding the content and implications of the recommendations in respect of depreciation and modernisation (pgs. 89 — 91) and audit committees (pgs. 99 — 100).

While it is true that the income tax concessions for depreciation are meant for replacement, it is also necessary to remember that the depreciation provision and investment allowance, etc., are among the principal sources of cash retention. They also therefore, provide sources of margin for working capital. The provision for depreciation, etc, cannot therefore be viewed in isolation purely for replacement of plant and machinery. The recommended insistence on segregation and investment in a specified manner of the relevant provisions and reserves will create avoidable operational difficulties in the appraisal and obtention of working capital requirements. You might recall that certain restrictive measures of this kind were imposed by the late Shri T. T. Krishnamachari in or around 1958, and these had to be withdrawn soon. I am therefore opposed to establishing a linkage by law "between modernisation and the benefits allowed for the purpose". I am afraid that, together with the implementation of the Tandon and Chore reports, such compulsion will adversely affect both current operations as well as the growth even of healthy companies. I am not however opposed in principle to restrictions on dividends when surpluses for this purpose arise only due to the method of depreciation adopted by the company concerned.

I feel that the recommendations in respect of a modernisation fund take what is intrinsically only a financial view of the problem. There are wider implications of location, technology and marketing which are germane to modernisation, and these cannot be ignored.

The suggestion regarding audit committees is constructive but the proposal as put forward in the report refers to an industrial unit rather than a company, even though the reference is to a committee of the Board of Directors. One of the companies with which I am as-

sociated experimented with an audit committee of the Board but, had to abandon the experiment because it was found that in practice the committee was looking into transactions and detailed comments from the internal auditors, rather than conducting performance audit in the sense understood, say, by the World Bank. Before such committees are contemplated either voluntarily or compulsorily in respect of companies listed on the stock exchange, present and future members of Boards would have to be appropriately educated in respect of the implications of audit of management performance. Without such an educative process even non-working directors can hardly be expected to fully realise what is expected of them in this novel and difficult task.

Once again, I deeply appreciate the courtesies that have been extended to me.

With regards,

Yours sincerely,
Sd/-
(R. K. Hazari)

Shri T. Tiwari,
Chairman,
I. R. C. I.



ANNEXURE — I

Names of Representative Bodies of Industry and Trade, Banks and Financial Institutions with whom the Committee held discussions

Name of the organisation 1.	Names and designations of the representing members 2.	Particulars of notes submitted 3.
1. All India Trade Union Congress (AITUC)	Shri T. N. Siddhanta, Secretary. Smt. Parvati Krishnan, Secretary.	i) "Industrial sickness — causes and remedies" — by Shri D. S. Nakra. ii) "Bonus and Tea Plantations" — by Shri K. P. Tripathi.
2. Indian National Trade Union Congress (INTUC)	—	Written views on the terms of reference of the committee, in response to the questionnaire.
3. Centre of Indian Trade Unions (CITU)	Shri Nrisingha Chakrabarty, Secretary.	Written views on the terms of reference of the Committee, in response to the questionnaire.
4. Hind Mazdoor Sabha (HMS)	Prof. Vinay Kumar, Secretary. Shri Mahesh Desai, Treasurer. Shri Brij Mohan Toofan, Secretary. Shri V. A. Khanolkar, Treasurer.	A note on industrial sickness.
5. Bharatiya Mazdoor Sangh (BMS)	Shri R. K. Bhakt, Secretary. Shri A. M. Puranik, Member, National Executive Committee.	Written views on the terms of reference of the Committee, in response to the questionnaire.
6. All India Manufacturers' Organisation (AIMO)	Shri K. V. Srinivasan.	Written views on the terms of reference of the Committee, in response to the questionnaire.
7. Indian Merchants' Chamber (IMC)	Shri N. C. Dalal.	Written views on the terms of reference of the Committee, in response to the questionnaire.

ANNEXURE — I (Concl'd.)

1.	2.	3.
8. Federation of Indian Chambers of Commerce and Industry (FICCI)	Shri D. B. Saxena	Written views on the terms of reference of the Committee, in response to the questionnaire.
9. The Associated Chambers of Commerce and Industry of India (ASSOCHAM)	Shri A. Sivasailam, President. Shri A. K. Sivaramakrishnan, Chairman, Committee on Direct Taxes, Shri C. Balakrishnan, Secretary.	i) Written views on the terms of reference of the Committee, in response to the questionnaire. ii) "Capacity Utilisation in Indian Industry" — by Tata Economic Consultancy Services. iii) Note on setting off of capital gains arising out of sale of assets of a unit against current and accumulated losses.
10. The Indian Banks' Association (I.B.A.)	Shri P. C. D. Nambiar, Chairman, IBA & SBI. Shri B. V. Sonalkar, Chairman, Central Bank of India, Shri N. Vaghul, Chairman, Bank of India. Shri R. R. Kumar, Chairman, Union Bank of India. Shri M. V. Subba Rao, Chairman, Indian Bank.	Written views on the terms of reference of the Committee, in response to the questionnaire. —do— —do—
11. The Inter-Institutional Meeting members (IIM members)	Shri N. N. Pai, Chairman, IDBI; Chairman, IIM. Shri B. B. Singh, Chairman, IFCI. Shri S. S. Nadkarni, Managing Director, ICICI. Shri M. J. Pherwani, General Manager, GIC. Shri S. Hariharan, Executive Director, LIC.	Written views on the terms of reference of the Committee, in response to the questionnaire.

ANNEXURE — II

Outstanding credit of scheduled commercial banks to large borrowers and to industry (large, medium and small scale units) and the share of former in the latter — Industry-wise.

(Rs. in crores)

Name of the industry	Outstanding credit of scheduled commercial banks to industry as at the end of December					
	1976	1977	1978	1979	1980	1981 (June)
(A) Total to industry*	7,192.81	7,514.42	8,561.96	9,863.28	11,555.09	12,221.61
(B) Of which to						
1. Engineering & Electricals	1,289.34	1,599.40	1,746.10	2,100.32	2,388.93	2,321.35
2. Iron & Steel	523.30	516.38	589.51	675.84	716.96	640.48
3. Textiles@	1,199.06	1,420.04	1,536.75	1,690.14	1,831.82	1,966.38
4. Chemicals	702.19	838.08	958.46	1,198.77	1,410.10	1,587.91
5. Jute	114.84	130.44	142.51	149.69	151.24	179.08
6. Sugar	154.72	192.82	275.61	206.27	147.61	247.80
7. Cement	63.97	64.90	81.54	93.26	124.92	126.70
8. Rubber	145.22	173.53	186.83	207.78	244.71	245.95

* 'Total to industry' includes data in respect of all the industries, Hence these figures will not tally with the total of the individual eight industries presented here.

@ Includes 'Coir products including coir fibre and yarn matting, carpets, etc.' and 'Handloom textiles and Khadi (spinning, weaving, dyeing, printing, etc.).

ANNEXURE — II (Contd.)

Name of the Industry	Outstanding credit of scheduled commercial banks to large borrowers@ as at the end of December						
	1976	1977	1978	1979	1980	1981	1982 (June)
(A) Total to large borrowers*	5,026.00	6,067.00	7,386.00	8,670.00	8,882.00	10,741.00	11,452.00
(B) Of which to							
1. Engineering & Electricals	1,242.00	1,009.00	1,109.00	1,278.00	1,427.00	2,101.00	2,089.00
2. Iron & Steel	247.00	220.00	213.00	248.00	243.00	246.00	375.00
3. Textiles	696.00	784.00	855.00	919.00	995.00	1,222.00	1,195.00
4. Chemicals	366.00	431.00	493.00	590.00	706.00	810.00	948.00
5. Jute	85.00	130.00	129.00	126.00	124.00	130.00	135.00
6. Sugar	99.00	152.00	239.00	165.00	114.00	166.00	464.00
7. Cement	56.00	39.00	52.00	67.00	78.00	99.00	112.00
8. Rubber	89.00	114.00	123.00	191.00	137.00	141.00	152.00

* 'Total to large borrowers' includes data in respect of all the industries. Hence these figures will not tally with the total of the individual eight industries presented here.

@ Borrowers enjoying aggregate credit limit of Rs. 1 crore and above from the banking system are considered as large borrowers.

ANNEXURE II — (Concl.)

(Percentage)

Name of the Industry	Outstanding bank credit to large borrowers as percentage of outstanding bank credit to industry as at the end of December				
	1976	1977	1978	1979	1980
All Industries	69.9	80.7	86.3	87.9	76.9
Engineering & Electricals	96.3	63.1	63.5	60.8	59.7
Iron & Steel	47.2	42.6	36.1	36.7	33.9
Textiles	58.0	55.2	55.6	54.4	54.3
Chemicals	52.1	51.4	51.4	49.2	50.1
Jute	74.0	99.7	90.5	84.2	82.0
Sugar	64.0	78.8	86.7	80.0	77.2
Cement	87.5	60.1	63.8	71.8	62.4
Rubber	61.3	65.7	65.8	91.9	56.0

Sources : (i) For outstanding credit of scheduled commercial banks to large borrowers — Credit Authorisation Scheme, IECD, RBI.
(ii) For outstanding credit of scheduled commercial banks to industry-Basic Statistical Returns, DESACS, RBI.

ANNEXURE — III

Magnitude of Industrial Sickness in Large Sick Industrial Units:
State-wise and Industry-wise

I — State-wise

(Rs. in crores)

Name of the state	Outstanding credit@ of scheduled commercial banks to large sick industrial units as at the end of December					
	1976	1977	1978	1979	1980	1981
(A) Total to States	608.75	858.45	1,060.96	1,158.48	1,324.47	1,478.84
(B) Of which						
1. West Bengal	205.56	238.30	257.26	301.38	324.24	371.70
2. Maharashtra	144.98	199.54	269.51	273.41	323.25	341.86
3. Tamil Nadu	87.38	138.04	159.34	143.26	170.68	174.49
4. Gujarat	48.96	82.56	92.99	93.57	106.51	118.47
5. Uttar Pradesh	21.58	60.08	72.76	92.01	93.11	120.49
6. Karnataka	14.90	37.45	53.87	62.78	90.30	112.75
7. Bihar	14.93	17.03	25.06	35.32	33.67	33.53
8. Andhra Pradesh	12.93	19.21	25.14	33.59	34.90	41.55
9. Kerala	6.67	9.06	19.25	33.43	44.61	62.40
10. Madhya Pradesh	12.42	10.58	24.99	23.57	27.07	32.40
11. Orissa	10.66	13.48	17.34	18.48	21.73	13.43
12. Rajasthan	18.06	17.38	17.48	16.78	24.61	26.01
13. Haryana	3.73	7.62	8.47	10.10	7.22	6.36
14. Assam	0.38	1.41	2.13	2.35	2.67	2.50
15. Punjab	1.44	0.96	1.60	1.81	1.44	1.29
16. Delhi	3.29	3.12	7.19	9.94	8.29	6.68
17. Goa	0.88	1.03	4.77	4.83	6.03	8.48
18. Pondicherry	—	1.60	1.81	1.87	4.14	4.45

ANNEXURE — III (Concl'd.)

**Magnitude of Industrial Sickness in Large Sick Industrial Units :
State-wise and Industry-wise**

II — Industry-wise	(Rs. in crores)					
Name of the Industry	Outstanding credit@ of scheduled commercial banks to large sick industrial units as at the end of December					
	1976	1977	1978	1979	1980	1981
(A) Total to large sick industrial units	608.75	858.45	1,060.96	1,158.48	1,324.47	1,478.84
(B) Of which to						
1. Engineering and Electricals	241.27	225.78	256.96	320.24	316.91	321.79
2. Iron & Steel	—	41.57	56.45	73.58	94.76	99.97
3. Textiles	150.92	260.40	309.18	308.86	382.65	454.42
4. Chemicals	40.07	94.75	136.02	128.31	168.20	173.79
5. Jute	55.82	79.85	94.97	85.85	92.27	110.97
6. Sugar	18.08	40.49	70.10	79.62	64.06	74.44
7. Cement	13.35	10.90	14.70	13.23	13.21	14.52
8. Rubber	17.44	21.22	28.51	37.50	52.32	77.53

Notes : (i) Large sick industrial units are sick industrial units, individually enjoying aggregate credit of Rs. 1 crore and above from the banking system.

(ii) 'Total to States' includes data in respect of all the States. Hence these figures will not tally with the total of the individual eighteen states presented here.

(iii) 'Total to large sick industrial units' includes data in respect of all the industries. Hence these figures will not tally with the total of the individual eight industries presented here.

@ Includes non-fund-based credits.

Source : SIUD, IECD, RBI.

ANNEXURE — IV**Incidence of industrial sickness in the large sick industrial units :
Industry-wise**

(Percentage)

Name of the industry	Outstanding bank credit to large sick units as percentage of outstanding bank credit to large borrowers as at the end of December					
	1976	1977	1978	1979	1980	1981
1. All industries	12.1	14.1	14.4	13.4	14.9	13.8
2. Engineering & Electricities	19.4	22.4	23.2	25.1	22.2	15.3
3. Iron & Steel	—	18.9	26.5	29.7	39.0	40.6
4. Textiles	21.7	33.2	36.2	33.6	38.5	37.2
5. Chemicals	10.9	22.0	27.6	21.7	23.8	21.5
6. Jute	65.7	61.4	73.6	68.1	74.4	85.4
7. Sugar	18.3	26.6	29.3	48.3	56.2	44.8
8. Cement	23.8	27.9	28.3	19.7	16.9	14.7
9. Rubber	19.6	18.6	23.2	19.6	38.2	55.0

Note : Derived from the related figures presented in Annexures II and III, which also provide definitions and sources for the items in this Annexure.

ANNEXURE — V**Frequency distribution of sick units by combination of causes of sickness : Industry-wise**

No. of causes	Engineering including Iron & Steel and Electricals (146)		Textiles (44)		Sugar (44)		Chemicals (26)	
	No. of units	% to total	No. of units	% to total	No. of units	% to total	No. of units	% to total
Single cause	19	13.0	2	4.5	5	11.4	2	7.7
Two causes	31	21.2	6	13.6	28	63.6	8	30.8
Three causes	44	30.1	13	29.6	8	18.2	7	26.9
Four causes	40	27.4	19	43.2	3	6.8	6	23.1
Five causes	9	6.2	2	4.5	—	—	2	7.7
Six causes	3	2.1	1	2.3	—	—	1	3.8
Seven causes	—	—	1	2.3	—	—	—	—
Total	146	100.0	44	100.0	44	100.0	26	100.0

Figures in brackets indicate the number of sick units in the various industries covered in the analysis.

ANNEXURE — V (Contd.)

**Frequency distribution of sick units by combination of causes of sickness :
Industry-wise**

No. of causes	Jute (15)		Paper (9)		Cement (3)		Leather (5)		Pharmaceuticals (6)	
	No. of units	% to total	No. of units	% to total	No. of units	% to total	No. of units	% to total	No. of units	% to total
Single cause	3	20.0	—	—	—	—	—	—	4	66.6
Two causes	3	20.0	1	11.2	—	—	2	40.0	1	16.7
Three causes	3	20.0	4	44.4	—	—	—	—	—	—
Four causes	2	13.3	4	44.4	—	—	1	20.0	1	16.7
Five causes	3	20.0	—	—	1	33.3	—	—	—	—
Six causes	1	6.7	—	—	2	66.7	2	40.0	—	—
Seven causes	—	—	—	—	—	—	—	—	—	—
Total	15	100.0	9	100.0	3	100.0	5	100.0	6	100.0

ANNEXURE — V (Concl'd.)

No. of causes	Glass & Ceramics (7)		Hotels (8)		Others (28)		Total (341)	
	No. of units	% to total	No. of units	% to total	No. of units	% to total	No. of units	% to total
Single cause	—	—	—	—	7	25.0	42	12.3
Two causes	3	42.8	1	12.5	5	17.9	89	26.1
Three causes	2	28.6	3	37.5	10	35.7	94	27.6
Four causes	1	14.3	4	50.0	5	17.9	86	25.2
Five causes	1	14.3	—	—	—	—	18	5.3
Six causes	—	—	—	—	1	3.5	11	3.2
Seven causes	—	—	—	—	—	—	1	0.3
Total	7	100.0	8	100.0	28	100.0	341	100.0

Figures in brackets indicate the number of sick units in the various industries covered in the analysis.

ANNEXURE — VI

**Causes of sickness and percentage of units affected by each cause :
Industry-wise**

Causes of sickness	(Percentage)						
	Engineer- ing, electri- cals, Iron & Steel (146)	Textiles (44)	Sugar (44)	Chemicals (26)	Jute (15)	Paper (9)	Cement (3)
1. Management deficiencies/ mismanagement/ dissensions	61.0	72.7	65.9	65.4	46.7	88.8	100.0
2. Marketing constraints/ competitive market	28.1	6.8	—	46.2	93.3	11.1	—
3. Shortage of working capital/liquidity constraints	29.5	38.6	—	7.7	6.7	33.3	—
4. Power cuts	23.3	40.9	2.3	7.7	66.7	33.3	66.7
5. Labour trouble/ poor labour relations	30.1	22.7	—	11.5	20.0	22.2	33.3
6. Plant imbalance/ frequent break down/ obsolete machinery	17.1	47.7	2.3	23.1	40.0	33.3	—
7. Delays in project implementation	7.5	6.8	—	26.9	—	22.2	33.3
8. Raw material shortage/non- availability	11.0	6.8	90.9	19.2	—	22.2	100.0
9. Demand recession/ fluctuating market	18.5	45.5	—	11.5	20.0	—	—
10. Under utilisation of capacity	15.8	6.8	6.8	34.6	—	11.1	33.3
11. Cost overrun	4.8	4.5	2.3	23.1	—	33.3	—
12. Lack of quality control/inferior quality	5.5	—	4.5	—	—	—	—
13. High cost of production	11.6	29.5	27.3	3.8	—	—	—
14. Govt. controls/ adverse trading conditions/policy changes	17.8	—	—	3.8	13.3	—	33.3
15. High cost of inputs	—	—	13.6	—	—	—	—
16. Lack of technical know-how	3.4	6.8	—	15.4	—	11.1	33.3
17. Transport bottle- necks/location disadvantage	2.1	—	—	3.8	—	—	66.7
18. Sub-optimum product mix	1.4	2.3	—	—	—	—	—

Figures in brackets indicate the number of sick units in the various industries covered in the analysis.

ANNEXURE — VI (Contd.)

Causes of sickness	(Percentage)						
	Engineering electricals, Iron & Steel (146)	Textiles (44)	Sugar (44)	Chemicals (26)	Jute (15)	Paper (9)	Cement (5)
19. Unremunerative orders	4.8	—	—	—	—	—	—
20. High interest burden	0.7	4.5	—	—	—	—	—
21. Excess inventory	2.1	2.3	—	—	—	—	—
22. Non-viable operation	0.7	—	—	—	—	—	—
23. Non-availability of finance from banks and financial institutions	—	—	2.3	—	—	—	—
24. Poor resource management	—	—	2.3	—	—	—	—
25. Political situation	—	—	—	—	6.7	11.1	33.3
26. Unplanned diversification	1.4	—	—	—	—	—	—
27. Excess labour	—	—	—	—	—	—	—
28. Inadequate material management	0.7	—	—	—	—	—	—

ANNEXURE — VI (Contd.)

Causes of sickness	(Percentage)					
	Leather (5)	Pharmaceuticals (6)	Glass & Ceramics (7)	Hotels (8)	Other Industries (28)	Total (341)
1. Management deficiencies/mismanagement/dissension	60.0	66.7	57.1	87.5	67.9	65.1
2. Marketing constraints/competitive market	80.0	16.7	57.1	100.0	39.3	29.0
3. Shortage of working capital/liquidity constraints	40.0	16.7	57.1	37.5	17.9	23.8
4. Power cuts	20.0	—	42.9	—	10.7	22.6
5. Labour trouble/poor labour relations	40.0	16.7	42.9	—	25.0	22.3
6. Plant imbalance/frequent break down/obsolete machinery	20.0	—	28.6	—	25.0	21.1

Figures in brackets indicate the number of sick units in the various industries covered in the analysis.

ANNEXURE — VI (Concl.)

(Percentage)

Causes of sickness	Leather (5)	Pharma- ceuticals (6)	Glass & Ceramics (7)	Hotels (8)	Other In- dustries (28)	Total (341)
7. Delays in project implementation	—	—	—	50.0	7.1	8.8
8. Raw material shortage/ non-availability	20.0	—	—	—	14.3	21.7
9. Demand recession/ fluctuating market	20.0	—	—	—	10.7	16.7
10. Under utilisation of capacity	20.0	—	—	—	10.7	12.9
11. Cost overrun	—	—	—	50.0	21.4	8.5
12. Lack of quality control/inferior quality	20.0	—	—	—	—	3.2
13. High cost of production	20.0	16.7	—	—	—	13.5
14. Govt. controls/ adverse trading conditions/policy changes	20.0	16.7	—	—	—	9.4
15. High cost of inputs	—	—	—	—	—	1.8
16. Lack of technical know-how	20.0	16.7	14.3	—	—	5.0
17. Transport bottlenecks/ locational disadvantage	—	—	—	—	—	1.8
18. Sub-optimum product mix	—	—	—	—	—	0.9
19. Unremunerative orders	—	—	—	—	3.6	2.3
20. High interest burden	—	—	—	12.5	—	1.2
21. Excess inventory	—	—	—	—	—	1.2
22. Non viable operation	—	—	—	—	—	0.3
23. Non availability of finance from banks and financial institutions	—	—	—	—	—	0.3
24. Poor resource management	—	—	—	—	—	0.3
25. Political situation	—	—	—	—	—	0.9
26. Unplanned diversification	—	—	—	—	—	0.6
27. Excess labour	—	—	—	—	7.1	0.6
28. Inadequate material management	—	—	—	—	—	0.3

Figures in brackets indicate the number of sick units in the various industries covered in the analysis.

Causes of sickness of 18 selected units **ANNEXURE — VII**

Causes of sickness	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	XIII	XIV	XV	XVI	XVII	XVIII	Total No. of units affected by a cause
A. Financial factors																			
1. Cost overrun	—	—	—	—	—	—	—	—	Yes	Yes	Yes	—	—	—	—	—	—	—	3
2. High debt-service charges/interest rate	Yes	—	Yes	—	—	—	Yes	Yes	—	—	—	—	—	—	—	—	—	—	4
3. High wage structure	—	—	Yes	—	—	—	—	Yes	—	—	—	—	—	—	—	—	—	—	2
4. Non-availability of finance from institutions	—	Yes	—	—	—	—	—	—	—	—	—	—	—	—	—	Yes	—	—	2
5. Liberal divi- dend policy	—	—	—	—	—	—	Yes	—	—	—	—	—	—	—	—	—	—	—	1
6. Higher cost of inputs	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	Yes	—	—	1
B. Managerial factors																			
1. Ineffective/ineffi- cient management	—	Yes	—	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	—	Yes	—	Yes	—	Yes	—	12
2. Poor resource management/large investments in fixed assets/ excess inventory	—	Yes	—	—	—	—	—	Yes	—	Yes	—	—	Yes	—	—	—	—	—	4
3. Poor labour relations/labour troubles	—	—	—	—	—	Yes	—	Yes	—	Yes	Yes	—	Yes	—	Yes	Yes	Yes	—	8
4. Weak marketing arrangements/ poor performance of selling agents	—	—	—	—	—	—	—	Yes	Yes	—	Yes	—	—	Yes	—	—	—	—	4
5. Unviable/failure of diversification programme	—	—	—	—	—	—	Yes	—	—	—	Yes	—	—	—	—	—	—	—	2

Causes of sickness of 18 selected units ANNEXURE — VII (Contd.)

Causes of sickness										Serial Number of the Unit										Total No. of units affect- ed by a cause
I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	XIII	XIV	XV	XVI	XVII	XVIII			
C. Technical factors																				
1. Frequent breakdowns	Yes	—	—	—	—	—	—	—	—	—	—	Yes	—	Yes	Yes	—	Yes	5		
2. Under utilisation of capacity	Yes	—	Yes	—	—	—	Yes	Yes	—	—	—	—	Yes	—	Yes	Yes	Yes	9		
3. Lack of R & D efforts	—	—	Yes	—	—	—	—	—	—	—	—	—	—	—	—	—	—	1		
4. Lack of normal maintenance of plants	—	—	—	—	Yes	—	—	—	—	—	—	—	—	—	—	—	—	1		
5. Non-availability/irregular supply of raw materials	—	—	—	—	—	—	—	Yes	Yes	Yes	—	Yes	—	Yes	—	—	—	5		
6. Quality control defective	—	—	—	—	—	—	—	—	—	—	Yes	—	—	—	Yes	—	—	2		
D. Infrastructural factors																				
1. Erratic power supply/power cut	Yes	—	Yes	—	Yes	Yes	—	Yes	—	Yes	Yes	—	—	—	—	—	—	7		
2. Transport bottle necks	—	—	—	—	—	—	—	—	Yes	—	—	—	—	—	—	—	—	1		
E. Environmental factors																				
1. Government Controls/low retention prices	Yes	—	Yes	—	—	—	Yes	—	—	—	—	—	—	—	—	—	Yes	4		
2. Increase in indirect taxes	—	—	Yes	—	—	—	—	—	—	—	—	—	—	—	—	—	—	1		
3. Unfavourable market trend/market recession	—	—	—	—	—	—	—	Yes	Yes	—	—	—	—	—	—	—	—	3		
Total causes affecting a unit	5	3	7	2	3	3	4	10	5	8	7	1	5	2	4	6	4	3		

Causes of sickness of 15 selected units

ANNEXURE — VIII

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	XIII	XIV	XV	Total No. of units affected by a cause
A. Financial factors																
1. Cost overrun	Yes	—	—	—	—	—	—	—	—	Yes	—	—	—	—	—	2
2. Diversion of funds/ financial indiscipline	—	Yes	—	—	Yes	—	—	—	Yes	Yes	—	—	—	—	—	4
3. High wage structure/over- heads/over staffing	—	—	—	Yes	—	—	—	—	—	—	Yes	—	Yes	—	Yes	5
4. Liberal dividend policy	—	—	—	—	—	—	—	—	—	Yes	—	—	—	—	—	1
5. High prices of inputs/ raw materials	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—
6. High cost of power/ transport	—	—	—	Yes	—	Yes	—	—	—	—	Yes	—	Yes	—	—	6
7. High debt-service charge, interest rate, etc.	—	—	—	—	—	—	—	—	—	Yes	—	—	Yes	—	—	2
8. Financial constraints	—	—	—	—	—	—	—	—	—	—	—	—	Yes	—	—	1
9. Fall in advances from dealers/delay in sales realisation	Yes	—	—	—	—	—	—	—	—	—	—	—	—	—	Yes	2
10. Lack of control of bank on account	—	—	—	—	—	—	—	Yes	—	—	—	—	—	—	—	1
B. Managerial factors																
1. Ineffective/inefficient management	Yes	—	—	Yes	Yes	Yes	—	Yes	Yes	—	—	Yes	—	—	Yes	8
2. Centralisation of power	—	—	—	—	—	—	—	—	Yes	—	—	—	—	—	—	1
3. Labour troubles	—	—	—	—	—	—	—	—	Yes	—	—	—	—	—	—	7
4. Poor resources management	—	—	—	Yes	—	Yes	Yes	Yes	Yes	Yes	—	—	—	—	Yes	7
5. Poor marketing arrangements/ performances	Yes	—	—	—	—	—	—	—	—	—	—	Yes	—	—	—	2
6. Unviable diversification	—	—	—	—	—	—	—	—	—	—	Yes	—	—	—	Yes	2
	—	—	—	—	—	—	—	—	Yes	—	—	—	—	—	—	1

Causes of sickness of 15 selected units **ANNEXURE — VIII (Concl'd.)**

Causes of sickness		Serial Number of the Unit															Total No. of units affect- ed by a cause
I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	XIII	XIV	XV			
C. Technical factors																	
1. Technical problems/ frequent breakdowns	Yes	—	Yes	Yes	Yes	Yes	—	Yes	—	—	Yes	—	Yes	—	9		
2. Lack of R & D efforts/poor quality controls	—	—	—	—	—	—	—	—	—	—	Yes	—	—	—	1		
3. Poor maintenance of plant & machinery	—	—	—	—	—	—	—	—	Yes	Yes	—	—	—	—	2		
4. Lack of modernisation	Yes	—	Yes	—	Yes	—	Yes	—	—	—	—	—	—	—	4		
D. Infrastructural factors																	
1. Power cut/erratic power supply	—	—	—	—	—	—	—	—	—	Yes	—	—	Yes	—	4		
2. Non-availability/irregular supply of raw materials	—	Yes	—	—	—	—	Yes	—	—	—	—	—	—	—	2		
E. Environmental factors																	
1. Govt. controls/low retention prices	—	Yes	—	—	—	—	—	—	—	—	—	Yes	—	—	2		
2. Multiple & increases in taxes/ excise duty, withdrawal of subsidies/concessions	—	—	—	—	Yes	—	—	—	—	—	—	—	Yes	Yes	3		
3. Demand recession/ stiff competition	—	—	Yes	Yes	Yes	—	Yes	—	—	Yes	—	Yes	—	—	7		
F. Miscellaneous factors																	
1. Scarcity/large turnover of technical hands	—	—	—	—	—	Yes	—	—	—	—	—	—	—	—	1		
2. Drought/floods	—	Yes	—	—	—	—	—	—	—	—	—	—	—	—	1		
3. Others	—	—	—	—	—	—	—	—	—	—	—	—	—	—	—		
Total number of causes affecting a unit	6	4	3	6	4	8	4	6	8	5	7	5	6	4	6		

ANNEXURE — IX

**Review of Cells set up in the banks to tackle the
problems of Sick Industrial Units**

1. As referred to in paragraph 4.24, a review of the set-up, qualifications of the personnel, etc in the cells obtaining in the banks has revealed the following position :
2. Out of the total number of 77 banks which were requested to furnish the required data on their cells to the Secretariat of the Committee, 58 banks responded. Of these 58 banks, while 31 had at least one cell each, the remaining 27 did not have any cell as on 30th June 1982, the reason being that they were not financing any/or medium and large sick industrial units, as given below :

**Table 1 : Distribution of 27 banks by reasons for not
setting up the rehabilitation cells**
(as on 30th June 1982)

Reasons for not setting up the cell	No. of Banks
1. Not financing any/or medium and large sick units	21
2. Account Officers accountable and responsible for sick units	1
3. Advances/Credit department at headquarters monitors sick units	2
4. Consortium leader responsible for sick units	2
5. Information not available	1
Total :	27

3. More than half the number of 31 banks (which reported having at least one cell), had only single cell each. However, 4 banks, on the other extreme, had 16 to 20 cells each; while in each of the remaining 11 banks the number of cells varied between 2 to 15 (Table-2).

**Table 2 : Distribution of 31 banks by number of
rehabilitation cells**
(as on 30th June 1982)

No. of cells	No. of banks
1	16
2-5	3
6-10	4
11-15	4
16-20	4
Total :	31

In all as on 30th June 1982, there were 180 cells in the 31 banks, the average number of cells per bank having at least one cell works out to less than 6.

4. As on 30th June 1982, there were 1,237 medium* and large sick industrial units under the portfolios of 31 banks which, as discussed earlier, had 180 cells for monitoring, etc. of the sick industrial units. Thus on an average each cell was supposed to look after the work of rehabilitation, etc. of about 7 medium and large sick industrial units. The position, as on end of June 1982, of viability and rehabilitation scheme, etc. of these 1,237 sick units is presented in Table-3.

Table 3 : Position of viability and rehabilitation of 1,237 medium and large sick industrial units
(as on 30th June 1982).

1. Total number of medium and large sick units under the portfolios of 31 banks	—	1,237
2. No. of units found viable/potentially viable	—	756
3. No. of units for which rehabilitation schemes prepared	—	591
Of which		
4. No. of units fully revived	—	87
5. No. of units showing signs of revival	—	292
6. No. of units showing no progress/deterioration	—	212

5. As for the arrangements in the banks for conducting viability studies of the medium and large sick industrial units, under their respective portfolios, it is observed that till 30th June 1982, the maximum number of viability studies completed were by a pool of personnel consisting of staff from the rehabilitation cells, other staff from the banks, consultants and consultancy agencies. Next in importance, by number of viability studies conducted, are the staff of the rehabilitation cells, albeit for a relatively large number of sick industrial units, consultants were assigned the job of conducting such studies (Table-4).

However, going by the number of studies in progress as on 30th June 1982, it appears that the staff from the cells are involved in maximum number of them, while the combination involving bank's personnel, consultants and consultancy agencies occupy the next important position. It is also worth noting that the role of consultants/consulting agencies for independently conducting viability studies has very much been reduced at least as far as the viability studies in progress are concerned.

* Large unit is one individually enjoying aggregate credit of Rs. 1 crore and above from the banking system. Non-S.S.I. unit enjoying total bank credit of less than Rs. 1 crore is categorised as a medium unit.

Table 4 : Arrangements for conducting viability studies and position of the same in respect of medium and large units

(as on 30th June 1982)

Arrangements for conducting viability studies	No. of viability studies	
	completed till 30th June 1982	in progress as on 30th June 1982
1. by the bank's staff* from cell only	188	34
2. by the bank's staff* from outside cell	33	10
3. by consultants	119	2
4. by consulting agencies	48	4
5. by combination of 1,2,3 and 4	213	31

* Relates to officer category only.

6. Majority of the 29 banks giving their opinion on the existing arrangements for the conduct of viability studies of sick industrial units have stated that the existing arrangements are adequate (Table-5).

Table 5 : Opinion of the banks on existing arrangements for the conduct of viability studies

(as on 30th June 1982)

Opinion of banks	No. of banks
1. Arrangements adequate	— 23
2. Arrangements not adequate	— 6
Total :	29

The banks which in their opinion feel that the existing arrangements are not adequate, are of the view that by and large there are no specialised staff to conduct viability studies. Some banks have also expressed that consultants/consulting agencies often take unduly long time to complete the viability studies, thus creating constraints for the banks to take quick decisions for the rehabilitation of the sick industrial units. Suggestions have also come from some banks that the cells for rehabilitation of the sick industrial units are required to be strengthened by inducting professionals for undertaking techno-economic/viability studies and for preparing rehabilitation programmes even if it may mean evolving on the part of the banks their own consultancy services.

7. The following table presents the distribution of rehabilitation cells by the number of officer staff who man the cells.

Table 6 : Distribution of rehabilitation cells by number of staff*
(as on 30th June 1982)

No. of staff*	No. of cells
1	42
2	31
3	26
4	14
5	5
6 — 9	12
10 and above	2
Information not available	48
Total :	180

* Relates to officer category only.

It is worth noting that 42 cells out of 180 reported to be existing in the banks as on 30th June 1982, are having only one officer each while in another 31 cells, there are only 2 officers per cell. The number of officers is found to be between 3 to 5 in 45 cells and between 6 to 9 in 12 cells. Only 2 cells had 10 or more officers each. By and large it is observed that the number of officers posted in various cells is related to the number of sick industrial units under the charge of such cells.

8. Almost 80% of the officers looking after the work of the sick industrial units are posted to the rehabilitation cells on a full time basis, though a significant proportion (more than 15%) of the officers attend to other jobs in their respective banks in addition to looking after the work in the cells (Table-7).

Table 7 : Distribution of staff* by their nature of working in the rehabilitation cells
(as on 30th June 1982)

Nature of working	No. of staff*
1. Wholly in the cell	300
2. Partly in the cell	58
3. Details not available	16
Total :	374

* Relates to officer category only.

9. Based on the information made available, it is found that majority of the officers posted in the cell have general type of qualifications only, that too mostly at the graduation level; officers with technical qualifications and also those with managerial or accountancy background are relatively quite few as indicated in Table-8.

Table 8 : Distribution of staff* by qualifications

(as on 30th June 1982)

Qualifications	No. of Staff*	Percentage to total
(A) General qualifications :	51	13.6
1. Undergraduates	4	1.1
2. Graduates	34	9.1
3. Postgraduates	11	2.9
4. Combination of more than one qualification	2	0.5
(B) Technical qualifications	35	9.4
5. Doctors in Science	1	0.2
6. Engineering Degree/Diploma	26	7.0
7. Postgraduate/Doctorate in Engineering	4	1.1
8. Combination of more than one qualification	4	1.1
(C) Management qualifications	27	7.2
9. Management Degree/Diploma	6	1.6
10. Accounting Degree/Diploma	13	3.5
11. Legal Degree	5	1.3
12. Combination of more than one qualification	3	0.8
(D) Information not available	261	69.8
Total :	374	100.0

* Relates to officer category only.

10. The deficiency of the majority of the officers posted in the cells, being not technically qualified, is also not to be found compensated with the experience in the job requirement i.e. of dealing with rehabilitation proposals of the sick industrial units. In fact, almost one-third of the total number of officers posted in the cells had 2 to 5 years of such experience. While less than 10% of the officers had 5-10 years' ex-

perience of dealing with sick industrial units an equal proportion possessed less than 2 years experience in this regard (Table-9).

Table 9 : Distribution of Staff* by experience of dealing with rehabilitation proposals

(as on 30th June 1982)

Experience (years)	No. of staff*	Percentage to total
Less than 2	33	8.8
2 to less than 5	122	32.6
5 to less than 10	37	9.9
10 to less than 15	17	4.6
15 and more	9	2.4
Details not available	156	41.7
Total :	374	100.0

* Relates to officer category only.

11. As regards the different cadres of the staff (including officers) in the cells, almost 60% were officers in the junior cadre, 30% from the higher cadre in the category of middle or senior level officers as given in Table-10.

Table 10 : Distribution of staff by levels of responsibilities

(as on 30th June 1982)

Level of responsibility	No. of staff	Percentage to total
1. Clerical/Secretarial assistance	53	12.4
2. Junior level officers	252	59.0
3. Middle level officers	49	11.5
4. Senior level officers	72	16.9
5. Information not available	1	0.2
Total :	427	100.0

12. For a good proportion of reporting banks, the time taken for completion of the viability study works out to 2 to 4 months, no doubt in some cases the time taken is reported to be even more than 6 months. Likewise, preparation of rehabilitation programme and its implementation, according to sizeable proportion of reporting banks, takes about 2 to 4 months each (Table-11).

Table 11 : Distribution of banks by time taken for conduct of viability study, etc. in respect of medium and large sick industrial units

(as on 30th June 1982)

Time taken (months)	No. of Banks		Implementa- tion of re- habilitation programme
	Completion of viability study	Preparation of rehabilitation programme	
Less than 2 months	5	11	7
2 to 4 months	13	6	6
4 to 6 months	4	5	4
6 months and more	2	1	3
Information not available	8	9	12
Total :	32	32	32

CASES INSTITUTED BY BANKS

DATA

Year	Number of suits instituted during the year	Amount involved	Total number of suits pending as at the end of the year	Total amount involved	Recoveries made during the year	Total amount of law charges outstanding at the end of the year
INDIAN BANK :						
1978	2,793	419.32	11,091	1,175.31	32.93	109.38
1979	6,362	618.41	16,953	1,695.72	143.50	159.29
1980	6,578	715.22	23,320	2,359.67	64.83	224.51
PUNJAB & SIND BANK :						
				Total Amount Recovered	Expenditure on litigation Fees of lawyers	(Rs. in lakhs)
1978	158	81.61	16	9.66	1.56	4.00 appx.
1979	316	208.46	49	30.89	2.84	7.81 appx.
1980	345	170.35	20	5.35	3.29	8.27 appx.
NEW BANK OF INDIA :						
1978	43	81,51,145.13	23	7,06,148.69	81,704.37	1,74,368.05
1979	60	55,88,133.37	16	2,05,830.99	84,134.93	1,81,906.25
1980	78	1,36,53,864.25	7	6,450.00	1,34,976.38	2,64,365.52

ANNEXURE — X (Contd.)

Year	Number of suits instituted during the year	Amount involved	Suits Decreed	Total Amount Recovered	Amount of litigation	
					Fees of lawyers	Other exp.
STATE BANK OF SAURASHTRA :						
1978	361	30,785	77	8,276	548	(000's omitted) 520
1979	389	24,126	79	2,908	1,121	218
1980	968	13,760	194	5,566	496	471
SYNDICATE BANK :						
1978	8,585	9.54	1,597	2.03		(Rs. in crores) 1.15
1979	14,727	13.50	1,783	2.40		1.55
1980	10,822	15.02	2,541	2.75		1.57
STATE BANK OF MYSORE :						
1978	1,253	Not readily available	817	Not	Readily	Available
1979	3,416	—do—	2,155	Not	Readily	Available
1980	1,910	—do—	2,091	Not	Readily	Available
CENTRAL BANK OF INDIA :						
1978	9	2,94,396.71	2	62,525.02	1,948	11,130
1979	7	1,30,993.00	—	—	7,033	6,250
1980	8	8,48,996.00	2	8,265.00	675	893

ANNEXURE — X (Contd.)

Year	Number of suits instituted during the year.	Amount involved	Suits Decreed	Total Amount Recovered	Expenditure on Litigation	
					Fees of lawyers	Other exp.
CANARA BANK :						
1978	12,487	589.92	1,993	65.48	25.54	(Rs. in lakhs) 12.88
1979	21,962	907.46	3,952	92.72	41.33	20.11
1980	2,22,670	1,502.75	3,782	129.78	51.72	16.13
ALLAHABAD BANK :						
1978	464	190.38	134	97.78	3.56	(Rs. in lakhs) 5.62
1979	660	164.00	147	45.42	3.22	10.70
1980	548	964.15	196	317.05	3.47	14.13
STATE BANK OF INDORE :						
1978	66	1,067	13	592	32	(Rs. in thousands) 21
1979	113	2,681	28	499	22	70
1980	134	1,637	9	86	25	102
UNITED COMMERCIAL BANK :						
			(January 1975 to June 1980)		(Lawyers' & other expenses)	
	12,465	8,89,99,526.06	4,253	51,68,262.04	67,84,475.04	
DENA BANK :						
1978	939	842.0	275	26.89	8.97	(Rs. in lakhs) 10.92
1979	1,075	475.0	241	25.53	7.72	8.62
1980	962	937.0	226	229.0	10.72	9.03

ANNEXURE — X (Contd.)

Year	Number of suits instituted during the year	Amount involved	Suits decreed	Total Amount Recovered	Expenditure on litigation	Other exp.
					Fees of lawyers	
STATE BANK OF TRAVANCORE :						
1978	1,334	1,03,03,247.33	171	11,84,839.62	2,58,524.03	(Amount in Rs.) 3,87,850.37
1979	2,604	68,84,397.64	355	17,19,152.10	2,30,509.27	4,93,752.32
1980	3,255	1,36,25,918.25	522	16,72,793.99	3,81,110.25	14,13,858.82
BANK OF INDIA :						
1978	2,238	9,52,22,748.82	499	34,35,185.80	16,80,775.91	(Amount in Rs.) 29,34,762.05
1979	2,781	11,61,03,652.28	749	61,57,511.28	24,25,246.18	39,06,064.61
1980	2,945	6,29,66,340.42	1,042	1,15,10,245.97	17,82,837.82	33,21,504.43
UNION BANK OF INDIA :						
1978	1,537	280.40	735	30.39	13.78	(Rs. in lakhs) 23.68
1979	2,358	763.98	594	20.98	16.06	25.89
1980	3,269	498.24	639	23.04	16.19	27.98
ANDHRA BANK :						
					(Rs. in crores)	
1978	1,962	0.91	6	0.04	4.98	(Fees to lawyers & Other exp.)
1979	506	1.34	46	0.10	14.29	
1980	538	1.54	16	0.01	6.92	
STATE BANK OF HYDERABAD :						
1978	623	91,14,900.88	308	19,11,645.17	2,09,531.60	(Amount in Rs.) 4,85,289.51
1979	985	1,97,36,759.64	545	38,96,281.90	3,23,214.33	5,61,259.26
1980	2,046	2,90,28,617.09	741	50,37,774.25	5,19,787.33	7,60,176.60

ANNEXURE — X (Contd.)

Year	Number of suits instituted during the year	Amount involved	Suits Decreed	Total Amount Recovered	Expenditure on litigation	
					Fees of lawyers	Other exp.
BANK OF MAHARASHTRA :						
1978	1,217	2,19,12,440.64	300	11,05,161.21	8,29,497.94	(Amount in Rs.) 9,66,745.62
1979	1,783	3,49,53,399.98	501	37,14,195.24	12,13,181.34	15,71,843.32
1980	1,704	4,96,60,414.27	544	23,14,899.36	12,50,014.11	20,15,103.38
ORIENTAL BANK OF COMMERCE :						
1978	58	44,39,488.47		1,84,268.59		
1979	75	36,96,963.59		50,560.35		
1980	74	50,20,400.29				
INDIAN OVERSEAS BANK :						
1978	1,010	2,03,23,613	234	24,21,200	4,34,441	(Amount in Rs.) 5,44,712
1979	1,501	2,80,23,132	360	37,23,786	9,16,658	6,22,212
1980	1,777	3,52,81,667	296	21,38,238	7,42,085	5,32,139
STATE BANK OF BIKANER AND JAIPUR :						
1978	163	7,743	37	1,204	83	(Rs. in thousand) 409
1979	690	7,405	93	1,107	222	361
1980	886	8,048	123	458	257	412
CORPORATION BANK :						
1978	284	199.04	84	5.97	2.77	(Rs. in lakhs) 8.57
1979	319	117.70	124	13.37	1.60	3.57
1980	379	137.00	244	16.08	2.70	3.13

ANNEXURE — X (Contd.)

Year	Number of suits instituted during the year	Amount Involved	Suits Decreed	Total Amount Recovered	Expenditure on Litigation	
					Fees of lawyers	Other exp.
VIJAYA BANK :					(Amount in Rs.)	
1978	204	94,01,128.00	82	6,91,067.00	2,04,941.00	3,72,952.00
1979	269	1,22,04,139.00	93	11,08,332.00	4,15,143.00	2,59,617.00
1980	380	2,91,90,443.00	118	25,63,073.00	15,98,334.00	6,46,654.00
PUNJAB NATIONAL BANK :					(Rupees in lakhs)	
1978	4,561	2,946.99	Not available 705 1,313	155.69 632.57	** 22,05,224.40	
1979	5,998	4,284.38			** 48,01,459.18	
1980	7,562	4,358.06			** 53,161,047.43	
** Break-up of columns 6 and 7 is not available as all litigation expenses are debited to Law charges Account.						
STATE BANK OF PATIALA :					(Amount in Rs)	
1978	23	24,34,797.24	8	51,325.31	59,534.60	2,04,413.25
1979	460	37,11,026.59	49	3,76,726.53	1,11,586.74	1,74,150.42
1980	357	42,08,566.93	108	3,88,125.96	87,780.30	2,59,182.02

ANNEXURE — X (Contd.)

STATE BANK OF INDIA

Data in respect of 7 circles, viz. Madras, Lucknow, Hyderabad, Bhopal, Chandigarh, Bhubaneswar and Gauhati

(Rs. in thousands)

Year	Particulars of cases instituted		Particulars of cases disposed off		Expenditure on litigation	
	No. of cases	Amount Involved	No. of cases	Amount recovered	Fees of lawyers	Other expenses
1978	11,205	1,35,734	4,494	9,781	1,549	1,550
1979	11,210	1,23,542	2,573	11,128	1,659	1,826
1980	11,915	1,78,628	2,875	19,342	2,654	2,576
1981	20,376	1,77,160	2,633	15,244	2,756	2,605
Data in respect of entire SBI						
1978	16,631	3,15,840	5,861	19,832	4,837	4,388
1979	17,178	3,54,808	3,873	28,017	5,239	4,222
1980	19,787	4,18,359	4,935	36,040	6,295	6,389
1981	29,813	3,74,206	4,382	35,183	7,566	5,837

CASES INSTITUTED BY IFCL, IRCI & ICICI **ANNEXURE — X (Contd.)**

No. of suits filed by the Corporation	Amount involved (Rs. in lakhs)	Time generally taken to obtain decrees (broad time frame)	No. of decrees obtained	Decretal amount (Rs. in lakhs)	Remarks if any					
(Upto May 1982)										
16	747.10	4 to 10 years	4	82.40						
Number of suits pending	Amount involved (Rs. in lakhs)	Number of suits Decreed	Amount recovered (Rs. in lakhs)	Litigation expenses (Rs. in lakhs)						
(Upto May 1983)										
12	270.11	3	3.01	3.46						
				<table><tr><td>Court Costs.</td><td>Expenses of Security guard</td><td>Solicitors' & Advocates' fees</td></tr><tr><td>1.76</td><td>0.80</td><td>0.90</td></tr></table>	Court Costs.	Expenses of Security guard	Solicitors' & Advocates' fees	1.76	0.80	0.90
Court Costs.	Expenses of Security guard	Solicitors' & Advocates' fees								
1.76	0.80	0.90								

ANNEXURE — X (Concd.)

ICICI :

Year	Particulars of cases instituted.		Particulars of cases disposed off		Expenditure on litigation		
	No. of cases	Amount involved	No. of cases	Amount recovered	Fees to lawyers	Other expenses	
1.	2.	3.	4.	5.	6.	7.	
1978	2	Rs. 42 lakhs	2	Rs. 42 lakhs			Upto May 25, 1983 77,118.25
1979	1	Rs. 17.41 lakhs	1	Rs. 16.31 lakhs		51,338.00	
1980	5	Rs. 64 lakhs	2	(a) 1 suit has been settled for the sum of Rs. 1,23,583/- (b) In another suit a consent decree has been passed for about Rs. 23 lakhs which is to be paid by instalments. (c) In two matters preliminary mortgage decrees have been passed.		9,36,807.84	
1981	3	Rs. 319 lakhs	None though preliminary mtge. decree passed in one matter.	—			3,01,197.88
1982	2	Rs. 156 lakhs	none	—			1,17,314.17

ANNEXURE XI

Constitution and Functions of the Special Tribunals

At the lower level, depending upon the number of cases, in each district or in a division consisting of a number of districts, there may be an officer called the 'Bank Claims Adjudication Officer' to adjudicate claims.

At the State level, there may be a 'Bank Claims State Tribunal'.

At the apex level, there may be a 'CENTRAL BOARD FOR RECOVERY OF BANK DUES.' To start with, it may have a single bench consisting of a Judicial Member and a Technical Member and later if required it may have more benches. The senior-most member in the CBBD may be appointed the President of the Board. For administration, the executive power over the tribunals in the country shall rest with the President. Decisions relating to policy matters on administration may be taken by a forum consisting of the President and four Vice-Presidents: one for each zone (viz., North, South, East and West). The senior member amongst the tribunals in a zone may be appointed the Vice-President of the zone. In the absence of the President from the headquarters and the Vice-President in a zone, the next seniormost member in the headquarters and in the zone may be appointed the President of CBBD and Vice-President of the zone respectively.

After adjudication of claims, to implement the order and to make recovery through execution proceeding, there may be Recovery Officer attached to the Office of the Adjudication Officer.

The State Tribunals may consist of a Technical Member and a Judicial Member. It will administer and supervise the functions of the Adjudication Officer and the Recovery Officer. The senior member in the Tribunal and in his absence, the next member shall exercise the said authority. The CBBD will have the authority and control over the entire class of tribunals including the State Tribunals.

The Judicial Members in the CBBD and the State Tribunals shall be deemed to hold a judicial office within the meaning of Article 217(a) of the Constitution of India.

ANNEXURE — XI (Contd.)

The qualifications, mode of appointment of the Adjudication Officer, Recovery Officer, Technical Member and the Judicial Member to the Qualifications of CBBB and to the State Tribunals, their terms and conditions of service, establishment, etc. are given below :

Members

**1. CENTRAL BOARD FOR RECOVERY OF BANK DUES
JUDICIAL MEMBER**

For being appointed as a Judicial Member :

He must have held or has been holding the office of a Senior District Judge or a Senior Officer in the Indian Legal Service equivalent to the rank of a Senior District Judge or Senior Officer in Reserve Bank/State/subsidiary/nationalised bank or a financial institution in the position of Head of the Law Department. Legal Adviser or any other seniormost Law Officer drawing a starting basic pay of not less than that of the General Manager of a Nationalised Bank.

He should also have an aggregate experience of 20 years in any of the aforesaid fields and this can also include his experience for a part of the period as an Advocate.

TECHNICAL MEMBER

For being appointed as a Technical Member :

He must have held or should be holding an office of a Senior officer in the rank of the General Manager in a nationalised bank or an office in the Reserve Bank/State Bank/subsidiary or financial institution drawing a basic pay of not less than the starting basic pay of a General Manager in a Nationalised Bank.

He must have experience of not less than 20 years in the operational side.

**2. BANK STATE TRIBUNAL
JUDICIAL MEMBER**

For being appointed as a Judicial Member :

He must have held or has been holding the office of a District Judge or a Senior Officer in the Indian Legal Service drawing a starting basic pay of not less than a District Judge or a Senior Law Officer in the Reserve Bank/State Bank/subsidiary/nationalised bank or a financial institution drawing a basic pay of not less than that of a District Judge.

ANNEXURE — XI (Contd.)

He should also have an aggregate experience of 15 years in any of the aforesaid fields and this can also include his experience for a part of the period as an Advocate.

TECHNICAL MEMBER

For being appointed as a Technical Member :

He must have held or has been holding a senior position in a nationalised bank or an office in the Reserve Bank/State Bank/subsidiary or financial institution in a post drawing a starting basic pay of not less than that of a District Judge.

He must have experience of not less than 15 years in the operational side.

BANK CLAIMS ADJUDICATION OFFICER

For being appointed as a Bank Claims Adjudication Officer :

He must have held or has been holding office in a post of middle management level (Scale II) in a nationalised Bank or in an equivalent post in Reserve Bank/State Bank/subsidiary/financial institution.

He should have an experience of 6 years in the legal side.

RECOVERY OFFICER

For being appointed as a Recovery Officer :

He must have held or has been holding the post of an Officer in the Junior Grade (Scale-I) in a nationalised Bank or a post equivalent to that in Reserve Bank/State Bank/subsidiary/financial institution.

He should have experience of 4 years in the legal or operational side.

TERMS AND REMUNERATION

1. The Judicial and the Technical Members of the CBBT and the State Tribunals may draw the emoluments and perquisites of General Manager and Deputy General Manager respectively in a nationalised bank.
2. Bank Claims Adjudication Officer will receive the pay and allowances equivalent to that of an officer in the middle management (Scale II) level of a nationalised bank.

ANNEXURE — XI (Contd.)

3. Recovery Officer will receive the pay and allowances equivalent to that of an officer in the junior grade (Scale I) of a nationalised bank.

At the time of appointment, any person drawing higher emoluments than the aforesaid grades, may be given pay protection.

ESTABLISHMENT

Supporting staff may be provided by a bank/financial institution which may be designated for the purpose by the RBI in various places.

Likewise, the premises for locating the CBBB/State Tribunals/offices may also be provided by a bank/financial institution in the said manner.

OTHER TERMS

All the Members, officers may be appointed on regular stream or may be brought on deputation. To the extent feasible, the Bank Claims Adjudication Officer, Recovery Officer and the Technical Members may be drawn in the services on deputation since this will give them promotional opportunities in their regular stream.

For the sake of continuity of the administration of the class of tribunals, the Judicial Members may be asked to continue till retirement in the CBBB and the State Tribunals. If they continue without reversion, as a compensation, additional remuneration may be considered for members who have put in more than 5 years of service, etc. The same will also apply to Technical Members at their option.

The Central Government may, in consultation with the RBI decide and make the appointments at District/Division, State and apex levels.

The recovery through special process may be made not only from industries, large, medium or small scale, but also from the other borrowers like traders, etc. but excluding the agriculturists.

For recovery from all For recovery of the loans from agriculturists, the various State Governments have passed legislations or made arrangements pursuant to the Talwar Committee* recommendations which have been accepted and adopted by the RBI and the State Governments. After gaining experience with regard to the working of the proposed tribunals and after a study of the system adopted by the States for recovery of bank dues from agriculturists, a review

* Report of the Expert Group on State Enactments having a bearing on Commercial Banks' lending to Agriculture (published by the RBI in 1971).

ANNEXURE — XI (Contd.)

may be made after 5 years to decide whether the proposed tribunals should be entrusted or not with the recovery of the dues of banks from agriculturists.

The claim against small scale industrial units and against other borrowers/guarantors, say, upto a maximum pecuniary limit of Rs. 20 lakhs may be filed before the Adjudication Officer. Claims against the medium and large scale industrial units and District level against any borrowers for a sum over and above Rs. 20 lakhs may be instituted before the State Tribunals.

Officers, Above lakhs may be instituted before the State Tribunals.

before State

Tribunals

The institutions/borrowers can also initiate proceedings before the Tribunals for settlement of the other specified disputes pertaining to recovery.

Against the decision of the Adjudication Officer, there can be an appeal to the State Tribunal. Against that appellate decision, there will be no second appeal. Against the decisions (in original matters) of the State Tribunal, there can be an appeal to the High Court.

Against the appellate decision of the State Tribunal or the CBBD, there can be a reference to the High Court on questions of law.

On receipt of a claim or other application, the Officer/State Tribunal may issue a notice to the opposite party enclosing copies of petition, etc. The opposite party may be given a period of 15 days from the date of receipt of notice by him, to appear before the officer with a direction that he may file a written objection, if any. In case the opposite party requires more time, this may be given by the Officer/Tribunal if so satisfied; otherwise, on perusal of the petition and the opposite party's statements, the Officer/State Tribunal may proceed with framing of issues.

On the date fixed, the Officer/State Tribunal may receive evidence, oral or written, give a hearing and pass orders/judgement. Where the borrower/guarantor has executed/furnished the requisite documents like promissory notes or agreements for loan, advances, deed of hypothecation/guarantee, or declaratory form relating to the creation of charge and the balance confirmation certificate, once the execution of documents is proved the presumption should be that the documents are valid, charges

presump- documents like promissory notes or agreements for loan,
tions advances, deed of hypothecation/guarantee, or declara-
Rebuttable tory form relating to the creation of charge and the
balance confirmation certificate, once the execution of documents is proved the presumption should be that the documents are valid, charges

ANNEXURE — XI (Contd.)

have been created validly and the claim of the bank is admissible which is rebuttable by the borrower/guarantor through evidence. Since the burden of proof is on the opposite party, to safeguard the interests of the borrowers/guarantors against the errors or negligence of banks, it may be made obligatory on the part of the banks to furnish to the borrower/guarantor, every year, brief particulars of the dues outstanding. If the borrower/guarantor desires to have a break-up of the accounts, the bank should furnish the same.

The Bankers' Books Evidence Act, 1891 provides inter alia, that a certified copy of any entry in a banker's books shall, in all legal proceedings, be received as prima facie evidence of the existence of such entry. The provisions of the said Act have been made applicable to the IDBI and other statutory financial institutions. Provisions may be made for extending the provisions of the said Act to all the public financial institutions whether constituted under an enactment or incorporated under the Companies Act.

The Officer/State Tribunal may dispose of the case within a period of three months unless they are otherwise satisfied that for the reasons **Disposal to be recorded and in the interest of justice, time should be extended further for the disposal of the case.** **within three months**

For the disposal of appeals by the State Tribunals/CBBD also, a time limit of three months may be prescribed giving discretion to the State Tribunals/CBBD to extend the time if they so think in the interest of justice for reasons recorded in writing.

Orders passed by the Officer/State Tribunal/CBBD shall have the same force and validity as that of a decree passed by a civil court and **Orders** can be executed. **like decree**

The High court may also be requested to earmark a Judge specially for expeditious disposal of the references. The Central Government may **Expeditious ensure appointment of judges for the purpose in each disposal by High Court, of persons having background experience in dealing with the laws relating to banking and institutional finance.** **High Court**

ANNEXURE — XI (Contd.)

Differences, if any, between the Judicial Member and the Technical Member in a State Tribunal in deciding a case or otherwise, may be referred to the Vice-President of the Zone or his nominee (being a member of any other State Tribunal within the Zone). The Vice-President or his nominee may, after perusal of the written arguments and if so required by the party, after giving a hearing, give his verdict agreeing with the Judicial or Technical Member and the same will be binding. Likewise, in case of differences between the Judicial Member and the Technical Member of the CBBB, the matter may be referred to a retired High Court Judge from a panel which may be maintained for this purpose. The said Judge may follow the afore-said procedure and give his decision which will be binding. Specific honorarium as may be prescribed, may be paid to the judge for the services rendered in each case.

**Sorting
differences
of opinion
between
Members of
Tribunal**

All the execution proceedings whether they relate to adjudication of claims below the pecuniary limit of Rs. 20 lakhs or above and relating to enforcement of orders relating to other disputes may be initiated before the Adjudication Officer. The Adjudication Officer may be assisted in the execution process by a Recovery Officer attached to the office and in particular cases, through a receiver appointed.

Execution

The Adjudication Officer will have the authority in case of any obstruction in execution or disobedience of the order or if the secured property is being stolen or secreted away, to order arrest and detention in a civil prison, to attach and to sell the properties of the debtor/guarantor/third party holding the properties of the debtor, to realise the proceeds and distribute the same to the banks/financial institutions and to the persons entitled thereto.

**Powers to
safeguard
property**

The Adjudication Officer will have such power to distribute the sale proceeds to the banks and financial institutions, being secured creditors, in accordance with the inter-se agreement/arrangement between them and to the other persons entitled thereto in accordance with the priorities in the law. The detailed procedure for adjudication and execution, subject to what is stated above, may be prescribed on the lines of the procedure (with refinement) contained in the Public Demands Recovery Act and Income-Tax Act.

**Distribution
of Proceeds**

ANNEXURE — XI (Contd.)

During the execution, if there are any disputes, the same may be placed before the Bank Claims Adjudication Officer and his orders shall be carried out by the parties concerned. Where the properties are sold in execution, the purchaser should get the same free from encumbrances. However, where there are practical difficulties for sale of the property free from encumbrances, the Recovery Officer may place the matter before the Adjudication Officer for decision. After giving opportunity to the parties and hearing, the Adjudication Officer may in his discretion, decide to sell the property subject to such encumbrances as he might determine (the rest of the encumbrances being discharged out of the sale proceeds).

**Purchaser
to get title
free from
(or with
such) encum-
brances**

The said authorities and the Recovery Officer may also have the power to seek the assistance of the Chief Metropolitan Magistrate or the District Magistrate for enforcement of their orders. It may be provided in the legislation that the said authorities on receipt of such requisition, shall provide the required assistance for enforcement of orders in execution and afford protection to executing officials, etc. through the police.

**District
Magistrate
to assist**

To ensure that this speedy process is not abused by the authority in the banks by initiating action against a party due to any difference of opinion, etc. it may be provided, by way of administrative instructions, that recovery proceedings should not be initiated by the bank officials without obtaining approval of a higher competent authority. Details in this regard may be worked out by the Boards of the banks.

**Approval of
Competent
authority for
initiation of
recovery**

Likewise, in a case where multiple institutions are involved, prior clearance of the Lead Institution/Bank (nominated in the Inter-se Agreement) should be required to be obtained, before submission of recovery claims before the Adjudication Officer. These provisions may not be written in the legislation as this may give a handle to the opposite party. Therefore, issue of administrative instructions in this regard is suggested. Provision relating thereto may also be incorporated in the Inter-se Agreements/Arrangements between institutions.

**Where
multiple
institutions —
Lead Bank
clearance**

The establishment expenses, salaries, etc. may be shared by banks and financial institutions in a manner and proportion specified by the RBI. The RBI may pay/bear the salaries and expenses through the State Bank/Nationalised Banks and obtain reimbursement of the same from banks/financial institutions.

**Establish-
ment
Expenses**

ANNEXURE — XI (Contd.)

The legislation may also provide for other consequential provisions. It may give powers to Central Government to make rules and regulations regarding the functions of the CBB, State Tribunals, Adjudication and Recovery Officers.

Consequential provisions

The provisions of Article 323B of the Constitution are pertinent as it deals with the establishment of tribunals. Different opinions have been expressed regarding the scope of the Article. According to one opinion, creation of such tribunals will be contrary to the Article. According to another, the Article is indicative and Parliament has the power to enact law creating tribunals de hors the Article and such law, as per the proposal, will be valid also for the reason that the High Courts' jurisdiction (by way of appeal reference) over the tribunals is being retained and further, in view of the availability of such alternative legal remedy, it will also minimise the issue of writs by High Courts and consequential stay orders of proceedings. It is proposed that the other civil courts will have no jurisdiction over these matters.

Article 323B of the Constitution

From the data (Annexure-X), it may be seen that there is no reasonable ratio between the sum to be recovered/actually recovered and cost incurred therefor which was sometimes higher than recovery. Irrespective of any recovery, costs will have to be incurred and in West Bengal these are assessed in case of contest at 15% each towards cost of suits and lawyer's fees and in uncontested cases at half of those rates. The court fee ranges from 5% to 1% in Maharashtra and from 7.5% to 1% in Tamilnadu. In Maharashtra, the lawyer's fee is between 8% to 1% in contested cases and at $\frac{1}{4}$ of the said rate in uncontested matters and in Tamilnadu it ranges from 10% (small causes and lower court) to 0.5% (for Rs. 1 lakh and above), 0.5% to 1% (High Court cases) and 0.5% to 0.25% in High Court appeals.

Cost aspect of present litigation

Unlike other States, silver lining in West Bengal and Maharashtra relating to court fee is that the maximum amount payable is Rs. 10,000/- and Rs. 15,000/- respectively.

During the pendency, banks will have to pay the salaries of security guards. On an average, the costs in each case may work out to 15%. This will have multiple effect in case of appeal/second appeal, etc. Apart from such direct cost, the bank has to incur indirect cost towards loss of interest, as the bank (decree-holder) is not normally allowed interest

ANNEXURE — XI (Contd.)

of more than 6% per annum from the date of filing of suit till recovery and this does not cover the cost of raising the fund, let alone at the current rate, but even at the old rate. To get the benefit of the lower rate of interest for longer period, the debtors do indulge in delaying tactics by dragging the proceedings and more the delay more the loss to the bank. No doubt, by virtue of amendment made to CPC, the restrictive provision relating to rate of interest was modified. But the courts are following the practice of awarding 6% rate of interest in a number of cases.

A proposal was put forward by the Finance Ministry to reduce the cost of litigation and also to initiate measures to enable the bank managers to spend less time in courts and more time in developmental work. For that purpose, queries were made to the **Views of the Banks** banks regarding the advisability of engaging Government lawyers, common lawyers and paid lawyers by the banks. The banks in their replies, however, addressed themselves

mostly to the issue relating to the engagement of Government pleaders to deal with bank cases. Majority of the Nationalised Banks as well as the RBI expressed the view that such entrustment of work to Government pleaders will lead to concentration of work and consequential delays.

Syndicate Bank and State Bank of Saurashtra have suggested the establishment of separate tribunals for recovery of bank dues.

Bank of Maharashtra (BOM) appreciated the suggestion to have whole-time pleaders but stated that their Law Officials were handling the work departmentally and it reduced the cost.

After establishment of tribunals, the Bank Law Officers may represent and deal with the cases. Following the lead given by BOM, this can be done even now selectively in simple cases by asking **In simple cases banks to be represented by officers** the Law Officers to represent the institution. A corporate body can represent itself through its officers. Even otherwise, the law (Advocates Act, 1965 — Sections 24(1) (e) and 28(2) (d) and the rules of State Bar Councils) now enables a full time salaried Law Officer (required to act or plead in court on behalf of his employer) of a bank/institution, (being public corporation or a body corporate constituted by statute) to get himself enrolled as an advocate. It is also suggested that Law Officer and not bank manager/officer will appear regularly before the Officer/Tribunal. The bank manager/other officers may appear before the Officer/Tribunal only for the purpose of giving evidence

ANNEXURE — XI (Concl'd.)

and not otherwise. This will enable them to concentrate on developmental work. The bank managers/other officers are, no doubt, required to assist the Law Officers when required with facts, analysis, etc. The suggestion to appoint paid lawyers (like Asst. Public Prosecutors to represent the State in criminal cases) to appear on behalf of banks before Adjudication Officers merits consideration. However, where difficult issues and complicated questions of law are involved before such Officers, State Level Tribunals, CBBD and High Courts, other lawyers including senior counsel may be engaged.

The premises and secretariat for the Tribunals at several places may be provided by the institutions nominated by the RBI. To inspire confidence in the public, the premises should, however, be
Premises — separate from the regular office. In view of the use of
Secretariat the existing facilities, there will be no extra establishment cost in setting up Tribunals.

To have satisfactory data on recovery, the Adjudication Officers should give a half-yearly return to the State Tribunals which, in turn, should furnish a half-yearly return to the CBBD. The
Returns CBBD may publish and submit an annual report to the
regarding Central Government which can be an authenticated report
disposal regarding the progress in recovery.
of cases

सत्यमेव जयते

APPENDIX — I

A) — Memorandum dated 14th May 1981

RESERVE BANK OF INDIA
CENTRAL OFFICEINDUSTRIAL CREDIT DEPARTMENT
BOMBAY-400 001

MEMORANDUM

The Reserve Bank of India appoints the following persons to constitute a Committee to examine the legal and other difficulties faced by banks and financial institutions in rehabilitation of sick industrial undertakings and suggest remedial measures, including changes in the law.

- | | |
|---|----------|
| 1. Shri T. Tiwari,
(Chairman, Industrial Reconstruction
Corporation of India Ltd., Calcutta) | Chairman |
| 2. Dr. P. D. Ojha,
(Chief Officer,
Industrial Credit Department,
Reserve Bank of India, Bombay) | Member |
| 3. Shri R. Viswanathan,
(Chief Manager (Credit),
State Bank of India,
Local Head Office, Madras) | Member |
| 4. Shri R. Sreekrishnan,
(Chief Officer (Law),
State Bank of India, Bombay) | Member |
| 5. Shri Y. V. Sivaramakrishnayya,
(Executive Director,
Bank of Baroda, Bombay) | Member |
| 6. Shri K. L. Roy,
(General Manager,
United Bank of India, Calcutta) | Member |
| 7. Shri S. A. Naik
(Legal Adviser,
Industrial Development
Bank of India, Bombay) | Member |

APPENDIX — I (Contd.)

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|--|------------------|
| 8. Shri R. Jagannathan,
(General Manager,
Industrial Development Bank of
India, Bombay) | Member |
| 9. Shri D. N. Davar,
(General Manager,
Industrial Finance Corporation
of India, New Delhi) | Member |
| 10. Shri C. Chandrasekhar,
(In-charge, Legal Department,
Industrial Credit and Investment
Corporation of India Ltd., Bombay) | Member |
| 11. Shri M. N. Govindaraj,
(Deputy Chief Officer,
Industrial Credit Department,
Reserve Bank of India,
Central Office, Bombay) | Member-Secretary |
2. The terms of reference of the Committee will be as follows :
- i) To review the present policy framework (including legal provisions) within which banks/financial institutions can bring about a change in the management of industrial units assisted by them and to make recommendations as to the changes considered desirable with a view to ensuring that the industrial units operate viably.
 - ii) To review the existing criteria adopted by banks/ financial institutions in determining the suitability of a sick unit for revival and to recommend appropriate modifications therein, keeping particularly in view the need to have a reasonable time-frame for any programme of revival.
 - iii) To identify the main constraints in the matter of rehabilitation of sick units, the problems faced by the banks/financial institutions involved and to suggest remedial measures including amendments to the various statutes.
 - iv) To suggest measures including amendments to legal provisions which would facilitate the restructuring of the capital base of the assisted units.
 - v) To identify in a general way, what are the concessions which should normally be made by the various agencies involved in the

APPENDIX — I (Contd.)

revival, including management and workers, and in that context whether sick units should be burdened with obligations like payment of minimum bonus and implementation of various wage awards, etc. which may be having adverse effects on the rehabilitation programmes.

- vi) To suggest stand-by institutional arrangements, (other than nationalisation) for purchase of undertakings or shares in companies owning the undertakings, in the absence of private purchasers or in competition with them, in the case of viable units so as to protect to the maximum extent possible, the institutional funds already involved in the undertakings.
 - vii) To identify the factors inhibiting expeditious mergers of sick units with the healthy ones and to suggest remedial measures for expediting such mergers.
 - viii) In cases where it is deemed necessary to dispose of certain/all the assets of the units — to suggest legal measures including amendments to the Land Ceiling Acts, etc., so as to expedite the legal process for speedy realisation of the dues of the banks/financial institutions.
 - ix) To review broadly the difficulties faced by the banks and financial institutions in the case of units taken over by Government under I (D & R) Act, 1951 and to suggest remedial measures.
 - x) To make such other suggestions and recommendations which in the opinion of the Committee are expedient for speeding up revival of the sick units.
3. The Committee will devise its own procedure and may call for such information and organise such discussions as it may consider necessary.
4. The Committee may submit its report as early as possible.

Sd/-
(W. S. Tambe)
Executive Director
14-5-1981

APPENDIX — I (Contd.)

B) — Memorandum dated 16th September 1981

**RESERVE BANK OF INDIA
CENTRAL OFFICE
INDUSTRIAL CREDIT DEPARTMENT
CENTRAL OFFICE BUILDING
POST BAG 10080
BOMBAY-400 023**

MEMORANDUM

The Reserve Bank of India appoints the following additional persons to the Committee constituted by it in terms of memorandum dated 14th May 1981 to examine the legal and other difficulties faced by banks and financial institutions in rehabilitation of sick industrial undertakings and suggest remedial measures, including changes in the law.

- | | |
|--|--------|
| 1. Shri D. R. Mehta,
Joint Secretary,
Banking Division,
Department of Economic Affairs,
Government of India,
New Delhi. | Member |
| 2. Shri S. C. Mittal,
Joint Secretary,
Department of Company Affairs,
Government of India,
New Delhi. | Member |
| 3. Shri P. K. Ahuja,
Deputy Secretary,
Department of Industrial Development,
Government of India,
New Delhi. | Member |
| 4. Dr. V. K. Agarwal,
Deputy Legal Adviser,
Department of Legal Affairs,
Government of India,
New Delhi. | Member |

APPENDIX — I (Contd.)

2. It has also been decided to enlarge the terms of reference of the Committee so as to include the following :

- i) to consider the need for any special legislation, its contents and its legal feasibility;
- ii) to study the necessity and feasibility of promoting amendments to various laws (in their application to sick units) independently or consequential or supplemental to the special legislation; and
- iii) to consider the feasibility of recovery of the dues of the financial institutions and banks by adopting the summary procedure obtaining under the Public Demands Recovery Act or similar local laws.

Sd/-
(W. S. Tambe)
Executive Director
16.9.1981

O) — Memorandum dated 12th October 1981

**RESERVE BANK OF INDIA
CENTRAL OFFICE**

**INDUSTRIAL CREDIT DEPARTMENT
BOMBAY-400 001**

MEMORANDUM

The Reserve Bank of India appoints Dr. R. K. Hazari as a Member of the Committee constituted by it under the Chairmanship of Shri T. Tiwari, Chairman, Industrial Reconstruction Corporation of India Ltd., in terms of memoranda dated 14th May 1981 and 16th September 1981 to examine the legal and other difficulties faced by banks and financial institutions in rehabilitation of sick industrial undertakings and suggest remedial measures, including changes in the law.

Sd/-
(M. Ramakrishnayya)
Deputy Governor
12.10.1981.

APPENDIX — I (Concl'd.)**D) — Memorandum dated 7th August 1982****RESERVE BANK OF INDIA
CENTRAL OFFICE****INDUSTRIAL CREDIT DEPARTMENT
BOMBAY-400 001****MEMORANDUM**

A reference may please be made to the Memorandum dated 14th May 1981 regarding the constitution of a Committee under the Chairmanship of Shri T. Tiwari, Chairman, Industrial Reconstruction Corporation of India Ltd., Calcutta, to examine the legal and other difficulties faced by banks and financial institutions in rehabilitation of sick industrial undertakings and suggest remedial measures, including changes in the law. Shri S. Jayaraman, Joint Chief Officer, Industrial Credit Department, Reserve Bank of India, Bombay, is appointed Member-Secretary of the Committee in place of Shri M. N. Govindaraj, with effect from the 12th August 1982.



Sd/-
(P. D. Ojha)
Executive Director
7.8.1982.

APPENDIX — II

Committee to examine the legal and other difficulties faced by banks and financial institutions in rehabilitation of sick industrial undertakings and suggest remedial measures; including changes in the law

INTERIM REPORT ON THE ISSUE OF SPECIAL LEGISLATION

1. Introduction

1.1. Reserve Bank of India appointed in May 1981 a Committee under the Chairmanship of Shri T. Tiwari, Chairman, Industrial Reconstruction Corporation of India Ltd. (IRCI) to examine the legal and other difficulties faced by banks and financial institutions in rehabilitation of sick industrial undertakings and suggest remedial measures, including changes in the law. The names of members of the Committee and the terms of reference are given in Annexures-I and II respectively.*

1.2. The Committee at its first meeting held on 19th June 1981 considered, inter alia, the expediency of a special legislation to help banks and financial institutions in revival and rehabilitation of sick industrial undertakings speedily and successfully. It, therefore, constituted a Legal Sub-Committee under the Chairmanship of Shri S. A. Naik, Legal Adviser, Industrial Development Bank of India (IDBI) to study the provisions in various existing legislations so as to review (i) whether there are any inconsistencies in them, and (ii) how far such legal provisions impede the speedy implementation of rehabilitation programmes of sick industrial undertakings. In the light of this study and also having regard to the terms of reference of the Committee, the Legal Sub-Committee was requested to suggest suitable amendments to the various existing legislations or in the alternative, consider the need for a special legislation for the purpose of timely rehabilitation of sick industrial undertakings. The names of members of the Legal Sub-Committee are given in Annexure-III.**

1.3. Subsequently, at a meeting convened by the Government of India on 18th July 1981 under the Chairmanship of Shri R. N. Malhotra, Secretary, Department of Economic Affairs to consider, inter alia, the recommendations of the Report of the Working Group on the merger of sick industrial units (H. N. Ray Committee), it was decided that the Tiwari Committee already constituted by the Reserve Bank of India should consider the different aspects of the proposal for special legislation for creation of Special Authority

* Please see paragraphs 1.12, 1.13, 1.16 and 1.18 of main Report.

** Please see paragraphs 1.15 and 1.16 of main Report.

and procedures and that this Committee should submit an interim report on the subject, as early as possible. Accordingly, the terms of reference of the Legal Sub-Committee were formally enlarged as follows :

- (a) Need for a special legislation, its legal feasibility and its contents; and
- (b) Necessity and feasibility of promoting amendments to existing laws (in their application to sick units) independently of or consequential or supplemental to, special legislation.

1.4. The Committee considered the report of the Legal Sub-Committee at a meeting held on 3rd November, 1981 in Calcutta and in the light of the discussions, it finalised this interim report on the issue of special legislation.

2. Dimension and Magnitude of the problem

2.1. At the outset, it is necessary to broadly indicate the dimension of sickness which is stated to have affected the industrial fabric of the national economy. According to the data collected by the Reserve Bank of India, as at the end of June 1980, about 23,740 industrial units (out of which large* units number about 389) were considered by commercial banks as sick†, involving an aggregate amount of Rs. 1,745 crores in bank credit, the share of the large units being at Rs. 1,286 crores. As per the data collected and parameters followed by financial institutions, 208 large industrial units accounting for Rs. 317.50 crores by way of outstanding term loans were regarded as sick** at the end of December 1980. It has also been observed that sickness among the industrial units has increased over the years, involving substantial amount of credit from banks and financial institutions.

2.2 A compilation made by the Reserve Bank of India on the basis of opinion survey of commercial banks indicates the following principal causes of sickness among the large units :

* A large unit, for this compilation is one which has been granted credit facilities aggregating Rs. 1 crore and above by the banking system.

† Reserve Bank has defined a sick unit as one which has incurred cash loss for one year and, in the judgement of the banks, is likely to continue to incur cash losses for the current year as well as the following year and which has an imbalance in its financial structure, such as current ratio of less than 1 : 1 and worsening debt-equity ratio (total outside liabilities to net worth).

** A unit is considered sick by the financial institutions, if it has sustained cash losses continuously over a period of at least the last two years and the accumulated losses as per the latest available balance sheet exceed 50% of its paid-up capital plus reserves.

Position as on 31.12.1979		
	No. of Units	% to total
(a) Mismanagement/management deficiency (including diversion of funds, infighting, lack of marketing agency, etc.)	197	52
(b) Market recession	86	23
(c) Faulty initial planning and other technical drawbacks	52	14
(d) Labour trouble	9	2
(e) Other reasons (power cut, shortage of raw materials, etc.)	34	9
Total :	378	100

- 2.3 The Committee has also received 14 case studies relating to sick industrial units from financial institutions and banks. On a review of these case studies, it is observed that sickness in industrial undertakings has arisen on account of various factors such as diversion of funds, utilisation of short-term resources for long-term purposes resulting in inadequate working capital, liberal dividend policy, purchases of raw materials at higher than generally ruling market prices, non-availability of essential inputs, poor marketing arrangements and slow realisation of sale proceeds, lack of proper quality control and technical know-how, frequent break-downs because of poor maintenance, power cut, labour disputes, excess of workforce, lack of co-ordination within the management, etc.

II

3. Methods of Revival or Rehabilitation

- 3.1 Against this background of the growing dimension and magnitude of industrial sickness, we may consider the options that are available for rehabilitation or revival of sick industrial undertakings. These options may be discussed briefly under the following heads :

- (i) Change or take-over of management;
- (ii) reconstruction (including restructuring of capital and liabilities);
- (iii) merger/amalgamation;
- (iv) transfer on lease;
- (v) sale as a running concern;

- (vi) take-over by purchase of shares by a healthy unit; and
- (vii) liquidation of the company owning the sick undertaking and purchase of its assets.

3.2 As we have to focus our attention mainly on medium and large undertakings, we shall deal with units which are, or which are owned by, companies or co-operative societies. The legal provisions which have a bearing on the above options are found in the Companies Act, 1956, the Industries (Development & Regulation) Act, 1951 (I (D & R) Act), the Monopolies & Restrictive Trade Practices Act, 1969 (MRTP Act), the Industrial Finance Corporation Act, 1948 (IFC Act), the State Financial Corporations Act, 1951 (SFCs Act), Co-operative Societies Acts, Income-tax Act (Section 72 A), etc. The provisions of these statutes which are more relevant to the present study, are considered in this report under various heads.

4. Change or take-over of management

4.1 The classification in paragraph 2.2 above shows that the major cause for industrial sickness has been identified as management deficiency, including mismanagement. It has come to be recognised that honest, sound and efficient management is an input of great significance and relevance not only in the timely and successful implementation of an industrial project but also in its smooth running and performance.

4.2 Sickness attributable to management deficiency may be classified broadly in two distinct stages of the project :

- (a) sickness arising at the time of planning and during the implementation, and
- (b) sickness arising after implementation.

4.3 Sickness at (a) above may arise mainly due to :

- (i) underestimation of various items of cost of the project;
- (ii) distortion or inability to procure some vital information having a bearing on the viability of the project;
- (iii) failure to take adequate follow-up measures for timely implementation of the project, thereby exposing the project to cost escalation;
- (iv) diversion of funds through various means e.g. by overstating the cost of civil works, over-invoicing of plant and machinery, over-charging of preliminary expenses, contingencies, etc.

The commissions and omissions indicated above seriously affect a project in various ways by the time it reaches the stage of production, leading eventually to sickness which further aggravates if the management does not or is unable to take adequate and timely corrective steps to meet the situation.

4.4 Sickness attributable to the management in the post-implementation stage, may arise due to the following factors :

- (i) There is a tendency with the promoters to oblige their friends and relatives by appointing them to technical and other specialised posts on the financial and marketing side without having regard to their suitability, aptitude, etc.
- (ii) In a number of cases, the promoters have vested interests, through their friends and relatives, in the purchase of raw materials, stores, etc. Often the raw materials either do not conform to necessary quality standards or the price paid is ingeniously jacked up.
- (iii) Often since the finished products are sold through people connected with the promoters, considerable indulgence is given in recovery of sale proceeds. Heavy interlocking of funds necessitates borrowings at much higher levels involving larger expenditure on account of interest charges, thus eventually affecting the health of the unit.
- (iv) At times for obtaining quick returns, no adequate attention is paid, within the knowledge of the top management, for proper maintenance of the plant and machinery with the result that after the initial years, there is either a steep fall in production or the goods do not conform to the required quality standards. This creates marketing problems leading to sickness of the unit.
- (v) In the case of units dealing in highly sensitive commodities such as yarn, sugar, etc. some promoters indulge, at the cost of the company, in speculative activities with all the attendant consequences. In certain cases, raw materials intended for the production of the company are sold for speculative gains. Such unhealthy practices affect the finances of the units and aggravate their sickness.
- (vi) There have also been instances of companies engaging in production of certain items with a view to securing quick returns, ignoring in the process, production of other items which contribute to the profitability of the Company in the long run.
- (vii) Due attention is not always paid by most of the companies to make adequate market forecasts. This may lead to heavy

accumulation of stocks of finished products thereby affecting the liquidity and in turn, the health of the company.

- (viii) Ineptitude, incompetence or inexperience of the management leads to various ills such as lack of corporate planning, budgeting and forecasts, proper control at cost and profit centres, etc. All these not only bring about but also aggravate sickness.

- 4.5 The above setting is only illustrative for our report and the instances and circumstances narrated may not be taken as exhaustive for all events.
- 4.6 The role of the management in maintaining the health of the unit being so crucial, it follows that if in respect of any unit, mismanagement or inefficient management has been found to be responsible for its sickness, the rehabilitation agency should be able to revamp the management. If the ultimate decision is to change the management, a view has to be taken about the tier of management at which the change is required. To the extent it is relevant in this context, the management of a company consists of two tiers, namely (i) Board level, and (ii) Executive level. As regards the Board level, normally changes in the membership of the Board can take place by resignation, retirement by rotation, or by removal. If a member of the Board, whose continuance is regarded as undesirable, refuses to vacate office by resignation, there can be only two options, i.e. either to wait till he retires by rotation or else to remove him. In terms of section 284 of the Companies Act, the general body can remove a director before the expiry of his term of office, by passing an ordinary resolution. Such resolution can be passed only after giving a special notice of the proposed resolution to all the members of the company. The director proposed to be removed is entitled to have his representation against the proposed resolution circulated in advance to the members and is also entitled to be heard at the general meeting. Thus, apart from the rehabilitation agency being required to muster more than 50% of the voting power, the process involved in removing a director from office turns out to be time consuming. Further, the process also gets stalled often by interested parties obtaining stay orders from the Courts. Likewise, in a case where a director retiring by rotation, who is considered undesirable, offers himself for re-election, the rehabilitation agency has to muster more than 50% of the voting power to ensure that such retiring director is not re-elected.
- 4.7 No doubt, financial institutions holding 50% of the total voting power in a company on the basis of ownership of share capital, can initiate changes at the Board level in terms of section 284 of the Companies Act. But if the institution is a limited company

like ICICI or IRCI, the company (owning the sick undertaking) in which the financial institution holds, by way of ownership, more than 50% of the share capital, will be deemed to be a subsidiary of such financial institution. In terms of section 212 *ibid*, such financial institution, being the holding company, will be required to annexe to its balance sheet, its subsidiary company's balance sheet, profit & loss account, etc. But the preparation of the annual accounts of a sick unit is invariably delayed as its working systems are variously affected. For want of audited accounts of the assisted sick unit, the presentation of the annual accounts of the financial institution would also get delayed. Such delay in presentation of the annual accounts of the financial institution and in consequence, the delay in convening its Annual General Meeting attract penal provisions against the directors and other officers of the concerned financial institution. This aspect acts as a deterrent to such financial institution for acquisition, by way of ownership (through market or by conversion of loan into equity), of more than 50% of the share capital in an assisted company with a view to controlling its affairs or management.

- 4.8 There is yet another mode by which change in the management can be effected, namely, by controlling the voting power through exercise by the institutions of the right to convert their loans or debentures into equity or through acquisition of shares in the market or through acquisition of sufficient proxy strength. Under section 81 (3) (b) of the Companies Act and the rules framed thereunder, conversion of loans of public financial institutions into equity at par or at a premium not exceeding 25% of the face value does not pose much difficulty. In case of sick units, obviously the shares cannot be converted at par, because of erosion in the net worth which is often negative. In such cases, the conversion will have to be at the intrinsic value of the shares which will normally be at a discount. If, therefore, the loan is to be converted into equity shares at a discount, then the procedure prescribed under section 81 (3) (b) *ibid* regarding special resolution of shareholders (75%) and approval of Central Government has to be complied with, in addition to the stipulation under section 79 for issue of shares at a discount. Regarding the acquisition of sufficient proxy so as to change the management, it depends on the co-operation of various shareholders; this may not always be forthcoming as this will be dependent on their interest in the continuance or discontinuance of the existing management. Again, in a case where the shares are widely dispersed, it will make the task further difficult. Similarly, acquisition of shares in the market for this purpose is also difficult.

- 4.9 Under section 408 of the Companies Act, the Government has also power to effect a change in the Board of Directors. But this power is, by law, limited only to making appointment of new directors on the Board and does not extend to removal of any of the existing directors. Further, even though the Government can exercise this power suo moto also, it can be exercised only on the Government being satisfied that appointment of such directors is necessary for the purpose of preventing the affairs of the company being conducted in a manner oppressive to any members or prejudicial to the interests of the company or to public interest. Thus, the exercise of this power by the Government has its limitations in view of the limited objectives of the provision.
- 4.10 As regards a change at the Managing Director's level, normally the Board of Directors enjoy the power to remove a Managing Director and the rehabilitation agency can cause this power to be exercised if it is in a position to control the Board as such. But, though removed from the Managing Directorship, such person would normally be entitled to continue as an ordinary director thereby necessitating recourse to the procedure of section 284 of the Companies Act, as mentioned in paragraph 4.6 ante, before he can be finally made to quit the Board. Then again, such person may normally enjoy the loyalty of the staff, by virtue of which he could continue to create problems to the new management.
- 4.11 Another way by which change in the control of management can be brought about without changing the existing management personnel is through dexterous use of the right to appoint nominee directors on the Board of the company conferred on IDBI, IFCI and SFCs under their statutes and pursuant to contractual arrangement with the company. Such a right can also be used in a restricted way by ICICI, IRCI and commercial banks under a right conferred in terms of the loan agreement entered into with the company, provided its Articles of Association enable the same.
- 4.12 As regards, a private limited company, unless the change of management is brought about voluntarily it can be resisted effectively by the existing management and the other interested parties in view of the restrictive character of a private limited company and the consequent limitations under the Companies Act regarding share transfer and management pattern.
- 4.13 As compared to the changes at the Board level, changes at the Executive level can be effected without involving much of a legal procedure. Even where some of the executives have a fixed term of office, their services can be terminated, pursuant to the terms of contract. This remedy can be resorted to only when the Board

of the concerned company co-operates with the rehabilitation agency.

- 4.14 It would thus be observed that while changes at the executive level do not pose much problem, any proposal for change in the more important tier, namely, the Board level, is difficult because of the cumbersome procedures of the Company Law, apart from the need and exercise involved in mustering adequate voting power required for carrying through such a proposal. Further, in such cases, stay orders are often obtained by interested parties preventing a smooth and timely change-over.
- 4.15 In relation to industrial undertakings run by co-operative societies it is necessary to mention of the manner in which the management of a co-operative society can be changed. Under the Co-operative Societies Acts of various States, the management of every society vests in a duly constituted Committee. The power to supercede the Committee is normally vested in the Registrar of Co-operative Societies of the concerned State. The Registrar can remove the Committee if it persistently makes default, or is negligent, in the performance of its duties or commits any act which is prejudicial to the interests of the Society or its members or disobeys Registrar's directions. After supersession of the Committee, the Registrar can appoint a new Committee in its place or appoint administrator to manage the society's affairs for a specified period not exceeding 4 or 5 years in the aggregate.
- 4.16 Under the Co-operative Societies Law, power is vested with the Registrar to supercede the management of the co-operative society for the purpose of improving the financial health and working of the undertakings. The problem relating to the application of this procedure seems to be in the lack of systematic approach in tackling industrial sickness.
- 4.17 The power to take over the management of an industrial undertaking and/or of the concern owning such undertaking (whether such concern is a company, a co-operative society or otherwise) is also contained in some special statutes like IFC Act and SFCs Act. In terms of section 28 of IFC Act, Industrial Finance Corporation of India (IFCI) has the right, inter-alia, to take over the management or possession or both of an industrial concern. This power is exercisable when an industrial concern assisted by IFCI makes default in repayment of any instalment of loan or otherwise fails to comply with the terms of its agreement with IFCI. In terms of the provisions of section 30-A to 30-E of IFC Act, as soon as the management of an industrial concern is taken over, IFCI is empowered to appoint as many persons as it thinks fit

to be the Directors of the industrial concern. All present Directors including the Managing or whole-time Director of industrial concern vacate their office without being entitled to any compensation for the loss of office. The Directors so appointed by IFCL are authorised, subject to control of IFCL, to manage the business of the industrial concern and to exercise such powers and duties as may be prescribed.

4.18 There are shortcomings in relation to the application of the above provisions, e.g.

- (i) The power available under section 28 of IFC Act is to take over the management or possession or both of an assisted industrial concern as a whole, and not of any particular undertaking(s) de hors the industrial concern.
- (ii) No procedure has been laid down or guidelines prescribed for taking over such management or possession. In case of resistance or obstruction, IFCL will perforce have to seek intervention of the Court which would mean time consuming litigation and delay causing further and costly deterioration in the health of the industrial unit.
- (iii) There is also no provision for freezing of the liabilities of the industrial concern after the management is taken over by IFCL, although there is an enabling provision for moving the Court for variation or cancellation of any contract. Necessary orders can be passed by the High Court, if it is satisfied after due enquiry that such contract has been entered into in bad faith and is detrimental to the interests of the industrial undertaking. No doubt IFCL, like any other financial institution, is free to approach the concerned State Government to declare the unit as a Relief Undertaking. It may be noted, however, that the law relating to Relief Undertaking is not in force in all the States. Further, a unit cannot qualify for such relief unless the State Government or a state-level agency has granted financial assistance to, or furnished guarantee on behalf of, the said unit. It is unlikely that all the industrial concerns would have taken such financial assistance.
- (iv) The power to take over management can be exercised even if there is a single default in repayment of any instalment of the loan or a breach of any of the terms and conditions of the loan. Thus, the underlying object seems to be to ensure recovery of the dues of IFCL. Obviously, provisions designed with this limited objective would not be of much assistance in reviving all types of industrial undertakings which are sick or show signs of incipient sickness.

- (v) In terms of IFC Act, the entire Board of Directors of an industrial concern cannot be changed without taking over the management.
 - (vi) In terms of section 28(4) *ibid*, when IFICI takes over the management or possession of an industrial concern, it is deemed to be the owner of that concern for the purpose of suit by or against such concern and accordingly, is liable to be sued in the name of such concern. This provision casts heavy and onerous responsibilities on IFICI.
- 4.19 Since sections 29 and 32A to 32F of SFCs Act are identical with the relevant provisions of IFC Act, the above observations made in relation to the IFC Act would also hold good in relation to SFCs Act. However, in case of IFICI, the powers under section 28 were invoked only in two cases, whereas in case of some State Financial Corporations, these powers have been extensively used.
- 4.20 Since a large proportion of the amounts recoverable from sick units is owing to commercial banks, it is relevant to consider at this stage the available legal framework for recovery of such advances by commercial banks. Special provisions on the lines found in the IFC/SFCs Act are available only to IFICI and SFCs. No such provision is available to other financial intermediaries, including commercial banks. Hence, commercial banks can have recourse only to the general law relating to creation and enforcement of security over the moveable and immoveable properties of the borrower.
- 4.21 As regards, the general law relating to the creation of security over moveable assets (including fixtures in the nature of machinery), the Banking Laws Committee has submitted a separate report.* Here, a scheme of legislation has been suggested to codify the law relating to hypothecation, pledge and other forms of security over moveable assets and fixtures. Special position of banks and financial institutions has been recognised in this scheme. This scheme allows the bank *inter alia*, to realise its dues by directly proceeding against the security without the intervention of Court. We understand that the scheme is already under the consideration of the Reserve Bank of India.
- 4.22 As regards the immoveable property of the borrower which may be offered as security in favour of commercial banks, the banks are required to follow the requirements of the mortgage law. The

* The Banking Laws Committee's Personal Property Security Law, 1977.

Banking Laws Committee in its report on Real Property Security Law (1977) has recommended* that banks should be statutorily vested with powers to proceed against the security without recourse to Court, whatever may be the form of the mortgage. There is also a recommendation that equitable mortgage should be confined only to banks and institutions, and a form relating to this type of mortgage should be filed with the Registrar of Assurances (so that anybody searching the records of the Registrar will come to know of the dues to the institution and of the charge in favour of the institution) as is presently done with the Registrar of Companies under Section 125 of Companies Act, 1956. Even after providing for the above, still, we have to point out that there are no provisions enabling banks or financial institutions to take remedial action for revival of sick units. In other words, the recourse of the banks is now confined only to proceed against the assets of the borrowing unit charged in their favour for realisation of dues. The Loan Agreement and the other loan documents obtained from the borrower do not enable the banks to deal with the undertaking and the persons in management. Of course, banks or financial institutions may move for the liquidation of the concern in default. Even if an order of liquidation is obtained, liquidation procedures are time consuming and complicated.

- 4.23 Hence, as of now, banks are also not in a position to exercise any of the options mentioned in paragraph 3.1 above for revival of a sick unit. Further, the nominee directors appointed by commercial banks by virtue of loan agreements do not enjoy such immunity against prosecution as available to similar directors of IDBI, IFCI and SFCs. Thus banks seem to be reluctant to appoint their nominee directors on the Boards of sick industrial undertakings. The aforesaid immunity is also not available to other financial institutions like ICICI, IRCI and State Industrial Development Corporations (SIDC).
- 4.24 The Banking Regulation Act, 1949 is regulatory in character and does not confer powers on banks to protect their interest from the point of view of recovery of dues or rehabilitation of sick industrial undertakings. Further, it is observed that section 19, *ibid*, is restrictive in character in that, no banking company can hold shares in any company as pledgee, mortgagee or absolute owner, of an amount exceeding 30% of the paid-up share capital of that company or 30% of the banking company's own paid-up share capital and reserves, whichever is less.
- 4.25 In view of the foregoing, this Committee is of the view that taking-over of the management under the existing provisions of

* Recommendations No. 21 to 23 of Banking Laws Committee.

IFC and SFCs Acts, and also by virtue of the agreements entered into with the defaulting industrial undertakings by banks and financial institutions, bristles with complexities and difficulties — legal and practical.

- 4.26 The only other law under which management can be changed is the I (D & R) Act. The power of the Central Government to order take-over of the management of an industrial undertaking is contained in sections 18A, 18AA and 18FA. The order for take-over under section 18A can be made only after an investigation into the circumstances relating to an industrial undertaking when there is (or likely to be) a substantial fall in its production or a marked deterioration in the quality of products or an unjustified rise in the price of its articles. Alternatively, such investigation may be ordered for the purpose of conserving any resources of national importance or when the undertaking is being managed in a manner detrimental to the industry or to public interest. On such investigation, if the Government is satisfied that it is necessary to issue certain directions to the undertaking, it may issue such directions regulating the production, prohibiting undesirable acts or practices, controlling the price or regulating the distribution, etc. If the undertaking commits default in complying with such directions the Government may order take-over of the management of the undertaking under section 18A. Under this section, management can also be taken over when the undertaking is being managed in a manner highly detrimental to the scheduled industry or to public interest.
- 4.27 An order of take-over without investigation can be made under section 18AA, only if by reckless investments or creation of encumbrances or diversification of funds a situation has been brought about affecting the production, or if the undertaking is closed for not less than three months. Even in respect of undertakings owned by companies in liquidation, Government can, subject to the existence of certain conditions, apply under section 18FA, to the concerned High Court for permission to take over management or control of the undertaking through an authorised person.
- 4.28 Experience has shown that situations do arise urgently necessitating the making of a serious bid for revival of an undertaking by taking over the management. But the nature of situations could be such that recourse to the provisions for take-over of the management might not be possible as hardly any of the conditions precedent to the applicability of those provisions could be said to exist. Also, in a few cases of management take-over under the Act, there have been legal challenges whether compulsive take-

over without requirements of natural justice being satisfied would be valid.

- 4.29 The provisions of I (D & R) Act have not proved effective for rehabilitation of sick units, nor in fact these provisions are designed for this purpose but only for the purpose of tackling errant units. Further, the machinery provided by the I (D & R) Act is presently not being used in relation to units which are not of certain minimum size. Besides, the Act itself applies only to scheduled industries keeping other industrial units out of its purview. It is neither all classes and types of sick undertakings nor all types of sickness which can be dealt with under the I (D & R) Act. Moreover, take-over of management under I (D & R) Act has not been effective mainly because it has not been possible to make substantial investment in fixed assets of the taken-over unit with a view to revamping it, without making structural changes. The question of final disposal of assets also comes up repeatedly and is considered in the dual context of changing ownership pattern and reducing excess liabilities, after which alone any further investment can be made to implement the basic revival scheme. Available alternatives, like reconstruction, sale as a running concern, etc., have generally been found unsatisfactory from many angles, and the only solution for future of such units has been found in their nationalisation. Government have recently decided that, in future, recourse to take over of management under the I (D & R) Act will be made only if the intention is to nationalise the undertaking. This will further reduce the effectiveness of the management take-over under that Act as an instrument for revival and rehabilitation of sick units.

5. Reconstruction and Merger

- 5.1 The second alternative, namely reconstruction (including restructuring of capital and liabilities) and the third alternative, namely merger, may be considered together, as they both are largely governed by the common provisions of the Companies Act.
- 5.2 Reconstruction of companies may comprise of restructuring of capital, that is to say, increase or reduction of capital, issue of different classes of shares, revaluation of assets, scaling down or writing off debts and liabilities, other compromise or arrangement with creditors and members, etc. Reconstruction of a sick undertaking or its merger with another unit can be given effect to under sections 391 to 394A of the Companies Act. In terms of section 391, the compromise or arrangement is required to be approved by the creditors/members (or by the concerned class of creditors/members), by a majority in number representing 3/4ths

in value. Thereafter, such proposal is required to be submitted to the Court and only after the Court has sanctioned the same, it becomes binding on all the creditors and members. Thus the two factors which normally stand in the way of speedily putting through any reconstruction scheme involving a compromise or arrangement with the creditors/members of an undertaking are : (i) very large number of the creditors/members required to approve of such a proposal, and (ii) elaborate legal procedure.

5.3 Briefly outlined below is the legal procedure required to be followed for formulating, putting through and implementing a scheme for compromise or arrangement with the creditors/members of a company or for its merger with another company.

- (i) The sponsors of such a scheme have to call class meetings under Court's directions. The Registrar of Companies settles the notices of the meetings and directs newspaper advertisements.
- (ii) In a merger proposal, both the transferor company and the transferee company have to obtain the sanction of the High Courts having respective jurisdiction and, where applicable, consents under FER Act and MRTP Act will have to be obtained.
- (iii) If the scheme involves reduction of capital or issue of fresh capital, confirmation/consent under the Companies Act, the Capital Issues Control Act, and, where applicable, also under FER Act and MRTP Act, may become necessary.
- (iv) The Court's order of sanction makes the Scheme binding on the dissenting creditors or members. For this purpose, the Court has to satisfy itself on the following, among other counts, before sanctioning the scheme —
 - (a) the prescribed procedure has been properly followed;
 - (b) a report from the Company Law Board or the Registrar of Companies that the affairs of the company have not been conducted in a manner prejudicial to the interest of its members or to public interest is received by the Court.
- (v) The aforesaid provisions can be made use of sparingly because of obvious conflict of interest between various classes of creditors, shareholders, etc., who are required to give their consent in 3/4ths majority for the purpose of approval of the scheme. The Court will have also to ensure that the members or creditors (or their relative class) were fairly represented by those who attended the meeting and that the statutory majority

were acting bonafide and not coercing the minority in order to promote any interest adverse to those of the class represented by them and that the arrangement is such as an intelligent honest man belonging to the class concerned or affected, might reasonably approve.

- (vi) In any such scheme, the Court will also consider its effects on the workers or employees to secure that, as far as possible, the scheme causes as little hardship as it can.
- (vii) While the Company Law gives the Court wide discretion to approve any kind of arrangement between the company and its shareholders, the Court has no jurisdiction to order stay of any criminal or revenue proceedings against the company; nor has the Court power to restrain a creditor from suing the company merely because a scheme is pending. This accounts for numerous petitions being filed with a view to thwarting the progress of a scheme.
- (viii) The Court has power to supervise the carrying out of the scheme and the terms of a scheme once approved can be changed only by a supplementary order of the Court.
- (ix) The Company law seems to be silent on the question whether the creditors of the transferor company would have an opportunity to represent their objection to the amalgamation. It is likely that the style of management of the transferee company may not be acceptable to the creditors of the transferor company or there may be other reasons to make them feel that their moneys may not be safe in the hands of the transferee company. This has special importance to the public financial institutions which may have advanced loans to the transferor company.

5.4 Although the above procedures are meant, by and large, for the protection of minority interests and dissentient creditors or members, in the general run of cases and taking all formalities from end to end, the procedure tends to be time consuming. Very often, the proceedings are intercepted by winding up petitions or petitions under section 397 or 398 alleging oppression of minority interest, engineered mostly by promoters and other vested interests. Sometimes, cross schemes are also submitted by certain interested parties mainly to thwart the original schemes and the courts are obliged to consider merits of both the schemes resulting in dilatory proceedings. The time taken for obtaining MRTTP and FERA clearances, wherever required, further aggravates the delays.

5.5 Under section 396 of the Companies Act, Government can, as a special case, without reference to the concerned High Court, order

merger or amalgamation of two companies in public interest. But there is a limitation in that sub-section (3) enjoins that every member or creditor of each of the companies before amalgamation shall have, as nearly as may be, the same interest in or rights against the company resulting from the amalgamation as he had in the original company. This condition is difficult of fulfilment in many cases with the result that the Central Government has not been able to resort to such amalgamation.

- 5.6 On an overall assessment of the experience with the concerned institutions, the above procedure under the Company Law is not considered to be responsive to the need for urgency and speed necessary for revival or rehabilitation of a sick industrial undertaking owned by a company.
- 5.7 In order to facilitate revival of sick industrial undertakings by their amalgamation with sound ones, a new section 72A was inserted in the Income-Tax Act, 1961 by the Finance (No. 2) Act, 1977 relaxing the provisions relating to carry forward and set off of the accumulated business loss and unabsorbed depreciation allowance, when the Central Government on the recommendation of the Specified Authority, is satisfied that certain conditions specified in this behalf are fulfilled. Even though the scheme was announced in 1977, only 51 effective proposals have been received by September 1981, of which 30 have been approved, 9 have been rejected and the remaining 12 are under consideration of the Specified Authority. With a view to encouraging effective use of this instrument, Central Government issued revised guidelines in February 1981 providing liberal approach for examination of the proposals by the Specified Authority. This also does not seem to have had any favourable impact so far, mainly due to the cumbersome procedures involved in merger/amalgamation. Approval of amalgamation by the Government under the Income-Tax Act, does not do away with the requisite compliance relating to the approvals by High Courts under the Companies Act, or by the Government under the MRTP Act, wherever applicable. Further, these approvals require considerable efforts and time, which a sick unit can ill afford. Even under the Income-Tax Act, approval under section 72A is denied if the total tax benefit is not required for implementation of the revival scheme, but only a part of it is justified.
- 5.8 In relation to co-operative societies (owning industrial undertakings), the State co-operative laws have made suitable provisions for reconstruction of societies. The proposal for a compromise or arrangement between a society and its members and/or creditors is required to be approved at a special general meeting called for

the purpose. Thereafter, on an application being made, the Registrar can order reconstruction of the society in the manner laid down in the Co-operative Societies Rules. These provisions are similar to sections 391 and 395 of the Companies Act, 1956. The Rules prescribe the precise manner in which such application has to be made to the Registrar. The Rules further provide that on the Registrar issuing an order approving reconstruction, the society shall stand reconstructed and the bye-laws of the society shall stand modified to that effect and to that extent.

- 5.9 The State Co-operative laws also contain elaborate provisions touching upon the following remedies : (a) amalgamation, (b) transfer of the assets and liabilities in whole or in part to other society, (c) division into two or more societies, and (d) conversion of a society into a society of a different class (say, conversion from a spinning society to a weaving society). Under the relevant provisions, two or more societies can, without dissolution, voluntarily amalgamate into one society. Some State laws also contain a provision for compulsory amalgamation. The effect of amalgamation under both the provisions is that assenting members of the original societies become members of the amalgamated society and further the assets and liabilities of the original society vest in the new society.
- 5.10 As regards the procedure for achieving the above result, the amalgamating society has to first obtain the approval of the Registrar to the proposal. Thereafter, at a special general meeting the proposal has to be approved by a two-thirds majority of the members present and voting. All the members, creditors and other persons whose interests are likely to be affected, have to be given an option to become members of the new society, or to continue their membership with the amalgamated or converted society, or to claim payment of their share or interest dues. The last mentioned provision creates a major obstacle because no funds are usually available with the sick amalgamating society with which such shares or interests could be purchased.
- 5.11 Once the scheme of amalgamation is approved by the Registrar, his approval itself results in sufficient conveyance of the assets and liabilities of the amalgamating society to the amalgamated society or to the converted society, notwithstanding the formalities or requirements of the Transfer of Property Act and the Indian Registration Act. This would facilitate easy conveyance of the assets and liabilities under the scheme of amalgamation and vesting them in the amalgamated society or the new society.
- 5.12 The Registrar has also the power to effect compulsory amalgamation, division or re-organisation of societies particularly for

purpose of securing proper management. The Registrar can provide for amalgamation, division or re-organisation and for vesting of properties, liabilities, dues and obligations, etc. in the new society (s). However, the section requires inviting objections of the society (s) within a period of not less than two months. After considering their objections, the Registrar may pass the order finally. A member or a creditor of each of the societies who objects to the scheme, is entitled to receive an amount in full satisfaction of his dues, contribution to share capital and interest.

- 5.13 Although recourse to the remedies available under the co-operative law can effectively help in the revival or rehabilitation of undertakings owned by co-operative societies, yet arbitration proceedings with the Registrar and suits filed in connection with matters 'touching the Society' do always delay and obstruct the smooth revival or rehabilitation.
- 5.14 As regards the position under the IFCI Act, there is no provision conferring any power on the IFCI to reconstruct an undertaking or arrange for its merger/amalgamation with another undertaking. This is because the powers conferred by that Act on the IFCI are for the purpose of recovery of its dues from the assisted concern, and are not designed for the revival of a sick unit. The same position holds good in relation to SFCs also. Similarly, commercial banks also do not enjoy any statutory powers for reconstruction of an industrial undertaking or its merger/amalgamation with another undertaking, as mentioned earlier.
- 5.15 As regards the position under the I (D & R) Act, there is no provision in that Act dealing with merger with the result that Government does not have power under that Act to bring about merger of a (sick) undertaking with another undertaking. However, Government can provide for reconstruction of an undertaking, the relevant provisions being contained in sections 18 FD, 18 FE and 18 FF, *ibid.* The condition precedent to invoking these provisions is that the Government should have first taken over the management or control of the industrial undertaking through an authorised person. Thereafter, in the light of the report made by the authorised person, if the Government is satisfied, *inter alia*, that in order to secure proper management of the company owning the undertaking, it is necessary to prepare a scheme for its reconstruction; the authorised person may be required to prepare such a scheme. The scheme may contain provisions, *inter alia*, for the capital, assets, liabilities, etc. of the company on its reconstruction, any changes in the Board, reduction of the interest or rights of the members and/or creditors (excluding the post-take-over debts arising out of loans), payment to the creditors in

satisfaction of their claims/reduced claims, allotment to the members of shares or payment in cash to them in satisfaction of their claims/reduced claims, conversion of any post-take-over debentures or loans into shares, increase of capital, etc. If the scheme is approved by the Government, a copy of the draft scheme is required to be sent to the company, to the creditors and to the registered trade unions of the employees and Government may modify the scheme in the light of their objections. Thereafter, the scheme requires to be approved by the High Court which has to afford an opportunity to the company, its members and creditors to be heard against the scheme. If the scheme is approved by the High Court (whether with or without modifications), it comes into operation whereupon the authorised person ceases to function and the management of the reconstructed company is assumed by the Board of Directors as provided in the scheme.

- 5.16 It has to be conceded that the power for reconstruction conferred on the Central Government by the above provisions is wide enough as to enable the Government to deal with any kind of situation or contingency arising in this connection. In fact, the provisions of the aforesaid section 18 FF show that the scheme for reconstruction can be framed in such a way as to touch upon any matter pertaining to the undertaking as pointed out in the preceding paragraph. However, the provisions of the I (D & R) Act for reconstruction of the undertakings have not been resorted to due to cumbersome procedures involved.
- 5.17 One legal provision which many a times acts as a drag on the proposal for merger or amalgamation of an industrial undertaking is contained in section 23 of the MRTP Act. In term of that section, if an industrial undertaking proposes to merge or amalgamate with another undertaking which is registered under the MRTP Act, or if the merger or amalgamation of two undertakings would bring into existence an undertaking which would be registerable under the MRTP Act, the proposal for such merger or amalgamation cannot be sanctioned by the Court unless it has first been approved by the Central Government. Experience shows that when an application is accordingly made to the Central Government it sets in motion a spate of submissions from many quarters raising various objections to such a proposal. Normally parties who have vested interest in such merger, etc. not taking place, set up other persons to raise objections to the proposal on various grounds. This naturally leads to the Central Government's approval being inordinately delayed, which causes a serious setback in the process of rehabilitation of a sick undertaking by its merger with another undertaking if the latter is owned by MRTP

company or if the merger would bring into existence an undertaking which would be registerable under the MRTTP Act.

- 5.18 In this context, the Committee examined the procedure adopted by the Reserve Bank of India for reconstruction and amalgamation of banking companies under section 45 of the Banking Regulation Act, 1949. This section empowers the Reserve Bank to apply to the Central Government for the grant of moratorium to a banking company where, in the opinion of the Reserve Bank, there are good reasons to do so, and to frame a scheme of reconstruction of the banking company or for its amalgamation with any other banking company. The schemes that may be framed by the Reserve Bank fall broadly under the following two categories :

- (a) amalgamation of an uneconomic or unsound banking company with another banking company;
- (b) reconstruction of two or more banking companies and their amalgamation to form one unit.

- 5.19 The scheme may provide for the appointment of a new board of the banking company on its reconstruction or of the above banking company with which it is amalgamated in accordance with the scheme. It may also provide for the reduction of the interest or rights which the members or creditors have in or against the banking company before its reconstruction or its amalgamation with other banking company. The draft scheme of reconstruction prepared by the Reserve Bank is required to be sent to the banking company and in the case of amalgamation also to the other banking company with which it is proposed to be amalgamated, for offering suggestions and objections, if any, within such period as the Reserve Bank may specify. The Reserve Bank may make such modifications in the draft scheme as it may consider necessary in the light of the suggestions and objections received from the banking companies and from their members or creditors. On finalisation, the scheme is submitted to the Central Government for sanction. After it has come into force, it is laid before both the Houses of Parliament.

- 5.20 The Committee noted that pursuant to exercise of powers under section 45 of the Banking Regulation Act, many unsound or uneconomic banking companies were reconstructed and/or amalgamated successfully with sound banking companies.

6. Transfer on lease or sale as a running concern

- 6.1 We may, considering the common aspect, deal with the options at (iv) and (v) mentioned in paragraph 3.1 ante together. These

options are — transfer on lease or sale as a running concern of the sick undertaking to another concern. In terms of section 293(1) (a) of the Companies Act, the Board of Directors of a company cannot sell or lease the whole or substantially the whole of its undertaking (or one of its undertakings if it owns more than one undertaking) without the consent of its general body. Since this consent has to be obtained in the form of an ordinary resolution, the proposal to sell or lease out the sick unit cannot be given effect to unless the reconstruction agency could muster more than 50% of the total voting power. Even if such consent is obtained for the lease, courts usually permit a lease only for a period of 2 or 3 years at a time. The reason is obvious in that a unit cannot be leased out for a longer period without reserving an opportunity of reviewing its operations at a short interval. Hence such an arrangement requires a constant review. It is likely that the lessee, unless it is a holding company or a subsidiary of the lessor, may enter into a lease expecting to retain an interest in the leased unit with an intent to acquire the control at the appropriate time. This might create conflicts between the lessor and the lessee, disrupting the functioning of the leased unit. This would, in turn, affect the schedule for payment of lease rent from out of which the outstanding dues of the financial institutions and banks are to be met.

- 6.2 As regards the co-operative sector, it is open to a co-operative society, as pointed out in paragraph 5.9, to transfer its assets and liabilities in whole or in part to another society, instead of amalgamating itself with another society. The procedure to be followed for this purpose is the same as in the case of amalgamation — briefly set out in paragraphs 5.10 and 5.11. Though the Co-operative Societies Act does not state so specifically, transfer on lease would also be covered by the above permissible provisions. In fact the Committee has come across an instance of a society having given its entire factory on lease to a limited company as this turned out to be more profitable.
- 6.3 Similarly, it seems open to a society to transfer a part of its undertaking by sale to another unit with a view to divesting itself of an unprofitable or sick undertaking or for improving its liquidity, etc. Thus, a sick society can perhaps adopt the course of leasing its undertaking or selling a part of its undertaking to overcome the phase of sickness.
- 6.4 The position under the IFC Act is fairly clear. In terms of section 28 *ibid*, IFCI has a right to transfer by way of lease or sale the properties charged to it by an assisted concern, when the concern commits defaults in repayment of loan or fails to comply

with any terms of its agreement with IFCI. However, this right of IFCI is limited to the property mortgaged, etc. to IFCI. Thus, IFCI does not seem to be expressly empowered to sell or lease the industrial undertaking as a going concern. As indicated in paragraph 4.18 (ii) ante, when exercise of this right by IFCI is obstructed, IFCI will have to seek intervention of the Court. Rest of the shortcomings in relation to the exercise of this power by IFCI have been briefly set out in paragraphs 4.18 (iv) and (vi) ante. The same position holds good under the SFCs Act also. However, banks do not have these powers. Hence they are required to seek any such remedies only through the Courts by virtue of the agreements entered into with the industrial undertakings and such a procedure is cumbersome, dilatory and expensive without desired results.

- 6.5 The powers given to the Central Government by the I (D & R) Act do not seem to extend to leasing out of the unit taken over to another concern. But Government can decide to sell it as a running concern, if in the light of the report of the authorised person, the Government is satisfied that the company cannot meet its current liabilities out of its current assets; Government would also decide that proceedings should simultaneously be started for the winding up of the company by the High Court. The authorised person has then to present an application to the High Court for winding up whereupon he would be appointed as official liquidator. On the basis of his report and the representations of the members and creditors, the Government has to determine the reserve price for the sale of the undertaking as a running concern. If the reserve price is not realised, the Government has to purchase the undertaking at that price. It is obvious from the foregoing that the Government may resort to the above course only when it is satisfied that the undertaking is beyond retrieval.
- 6.6 Some practical problems are also likely to be encountered in respect of certain cases, where attempts are made to sell the undertakings. The main problem relates to labour. Clause (c) of subsection (3) of section 18FE of I (D & R) Act provides that the authorised person, while submitting a report to Central Government as to what should be the reserve price should take into account the liability, inter alia, on account of terminal benefits to the employees. This means that unabsorbed employees have to be paid their terminal benefits from out of the sale proceeds. This, however, may not actually work out that way, in view of section 29D *ibid*, which provides for priority of payments to post-take-over loans and very often the sale proceeds may not be sufficient even to pay off such loans in full.

7. Take-over of a sick unit by a healthy unit by purchase of its shares

7.1 The last option is for take-over of the sick unit by a healthy one by purchase of its shares. In terms of section 395 of the Companies Act, shareholders of at least nine-tenths in value of the shares of the transferor company are required to approve of the take-over proposal. The merit of the scheme is that without resort to tedious Court proceedings the amalgamation or take-over is effected. In cases where dissentient shareholders exist, the procedure prescribed in the said section will have to be followed. In actual practice, however, it may be difficult for the company to secure such consent in view of the exceedingly large number of shareholders required to be won over to get such a proposal approved. Then again, sections 108A to 108H *ibid* also impose certain restrictions on acquisition or transfer of shares of/by an MRTP company.

7.2 The above provisions obviously stand in the way of the reconstruction agency making serious efforts for rehabilitation of a sick unit by purchase of its shares by a healthy unit. Often excess, undisclosed or unquantifiable liabilities of sick units are so large that the real value of shares becomes negative or indeterminate. Healthy companies would, therefore, be reluctant to acquire shares of such sick units unless adequate incentives are provided by the Government.

7.3 As regards sick units owned by co-operative societies, by the very nature of things, the remedy based on purchase of shares of a sick unit by a healthy unit may not apply to the co-operative sector. Since each member has only one vote, irrespective of his shareholding, there is no question of a single person or a unit purchasing the shares of another society with a view to securing its control. This remedy may not, therefore, be available for revival of a sick co-operative society, nor does it seem to be available under the IFC Act and the SFCs Act either.

8. Liquidation of the company owning the sick undertaking and purchase of its assets

8.1 Sometimes none of the alternatives discussed above becomes applicable and the sick industrial undertaking can be revived only through the liquidation of the company owning it and in the process, transfer of the undertaking to other entrepreneurs. Liquidation is presently covered by section 433 of the Companies Act and has to be approved by the High Court concerned. The procedure is dilatory and time consuming. Usually, there is a run on the company as a sequel to the liquidation proceedings leading

to unsecured creditors filing several petitions and dragging the company and also the secured creditors to the Court. In the meantime, the undertaking and its assets further deteriorate and the funds provided by banks and financial institutions remain blocked. There have also been instances where winding up of the company results into disintegration of the undertaking as the official liquidator finds that sale of different parts of assets to different purchasers would bring in higher realisations than by sale of the undertaking as a whole. It is, therefore, important that procedures are suitably changed so that the company can be liquidated summarily and the undertaking sold as a whole to other entrepreneurs so that it can be quickly restarted.

9. Contractual rights of financial institutions and banks

- 9.1 The financial institutions as also banks for the term loans normally reserve a contractual right in their loan agreement to take over the management of an assisted concern in the event of default. This is being provided as no statutory right is available to them (other than IFCI and SFCs) for such take over. This contractual right to take over management in case of default cannot be claimed to be a very effective method of rehabilitation of sick industries. Besides, the exercise of this right is rendered difficult and ineffective when it meets with resistance either from the promoter or management group or from the members or creditors of the company in relation to which this right is sought to be exercised.
- 9.2 One other contractual right of the banks and financial institutions that is relevant in this context is the right of sale of the property charged in their favour by a company as security for the financial assistance. Sale is either voluntary or involuntary, i.e., forced sale. We are here concerned with the latter kind of sale. Under the general law, the banks and financial institutions or, for that matter, any lenders, having a security in the shape of mortgage, charge or hypothecation of properties of an industrial concern, have the power to sell such mortgaged properties only, either by virtue of contract or by law and this may be done either with or without intervention of the Court, in certain circumstances. However, this power of sale is restricted to the mortgaged properties only does and not extend to the sale of an industrial concern, as a whole, as a running concern. Besides, sale of immoveable properties may require approvals from the concerned authorities, including the authorities under the Urban Land (Ceiling & Regulation) Act which takes considerable time. Therefore, the banks and financial institutions are not vested with adequate and effective power to enforce the sale of a sick unit as a running

concern to another concern, even when that is the only option open to rehabilitate a sick unit.

III

10. Need for a Special Legislation and, alternatively, feasibility of making amendments to existing laws

10.1 The above discussion would show that while the problem of sickness both in terms of its magnitude and trend is acute, the remedies to deal with sickness available under various statutes are inadequate so much so even many of the potentially viable sick units cannot be revived. Consequently, there is a loss of production and employment which our country can ill-afford. Besides, at present an amount of about Rs. 2,100 crores of banks and financial institutions is locked up in sick industrial units. Many of the difficulties in rehabilitating sick units arise since the various laws like the Companies Act, MRTP Act, etc. are not primarily meant to deal with the problems of sickness. Even if a statute refers to sick industrial undertakings or companies, approach is sectoral and from its own limited angle rather than based on a co-ordinated view. In such a situation, it is necessary to get out of the multiplicity of the existing laws and procedures and draw up a special legislation which will enable speedy and effective action to be taken for rehabilitation of the sick units. Such a legislation can create a specialised body exclusively devoted to revival of sick units, which step would ensure unified approach and speedy and time-bound decisions.

10.2 We are of the view that making of amendments to existing laws in their application to sick units as an alternative to the special legislative measure may not achieve the desired objective because it would require a large number of amendments, substantive as well as consequential, in all such statutes. Since various Acts have separate objectives, some of the amendments might not fit in their general schemes. Further, as pointed out earlier, a unified approach and concerted effort is necessary in the revival of a sick unit and accordingly, it would be advantageous to have a special legislation dealing with sick units.

11. Contents of the Special Legislation

11.1 Having examined the limitations of the existing legal framework vis-a-vis revival of sick units, we feel that the comprehensive special legislation, designed to deal with the problems of sickness, should provide for its objectives and basic parameters within which it should operate, remedies necessary for the revival of sick units, the body which should provide these remedies, its

procedures and other incidental matters required to make such legislation effective.

- 11.2 The question, viz., whether such a special legislation can form part of the existing statutes like Companies Act, I (D & R) Act, etc. has been considered. On an examination of the objectives of the various enactments, it is observed that Companies Act has been framed mainly to protect the interests of the shareholders and creditors. The I (D & R) Act was promoted to regulate the setting up of industries, their expansion and distribution of scarce commodities. Take-over of management of sick industrial undertaking figures in the context of maintenance of production and tackling the erring units. The objective of the Co-operative Societies law is mainly to regulate the co-operative societies and not that of the industrial undertaking, much less the sick industrial undertaking. There does not exist any comprehensive legislation dealing with the sick industrial undertakings and for their revival. In view of the magnitude of the problem of sick units and as the aforesaid Acts were enacted in different contexts, it is felt that a special legislation for the purpose of revival of sick industrial undertakings is essential, having regard to the factors like retention of employment, salvaging unused productive assets, utilisation of unused/idle capacity, recovery of public funds, etc. With a view to attaining these objectives, the application of certain enactments like Companies Act, MRTP Act, FER Act, etc. to the sick industrial undertakings and in the context of their revival will stand modified suitably for the purpose, in the larger public interests. सत्यमेव जयते
- 11.3 To be effective in dealing with the problems of sickness in industry, the special legislation should comprehensively provide for the following remedies necessary for the revival of sick units :
- (i) change or take-over of management;
 - (ii) reconstruction (including restructuring of capital and liabilities);
 - (iii) merger/amalgamation;
 - (iv) transfer on lease;
 - (v) sale as a running concern;
 - (vi) take over by purchase of shares by a healthy unit; and
 - (vii) liquidation of owning company and purchase of its assets.
- 11.4 While underlining the need for special legislation and before outlining its form and content, we would like to emphasise here that the special legislation should not divest the banks and financial

institutions of their responsibility to tackle the problems of sickness of the industrial units assisted by them. These agencies would have to make efforts for the revival of sick units within the ambit of the existing remedies and powers available to them whether under the statute or by covenants. As a supplemental expedient, the powers conferred on some of them could be modified or enlarged and those without it, could be conferred such powers to meet the exigencies of their revival effort. Only when they fail, they would seek the remedies under the proposed special legislation.

Change or take-over of management

- 11.5 Management take-over can be considered either for a limited period during which a proposal for change of ownership or for reconstitution is under consideration under this legislation, or for a temporary period of not more than 3 years which may be extended in special cases, by which time the financial institutions and other agencies concerned may submit appropriate remedies for consideration under this legislation.
- 11.6 Change of management can be brought about either by reconstitution of the Board of Directors if the sick undertaking is the only undertaking owned by the company or by appointment of authorised persons where the undertaking is one of a number of undertakings owned by the company. In certain cases, appointment of key personnel like Managing Director or certain officers can serve the purpose. New management can be generally provided by the financial institutions, and/or banks for which they may consider setting up necessary arrangements. The directors and officers so appointed should have the same protection as is available to the directors appointed by IDBI, IFCI, etc. under their respective statutes.

Reconstruction

- 11.7 A scheme for reconstruction of share capital or liabilities may provide a reasonable capital base, debt-equity ratio consistent with the expected return after reconstruction and rehabilitation. It may also contain provisions for issue of special share capital including shares at a discount to the public financial institutions carrying special rights as to voting, dividend and return of capital; transfer of the special capital by the financial institutions to any person (so as to enable him to provide the requisite management), redemption of the special capital at the specified point of time, etc.

Merger

- 11.8 Merger or amalgamation may be of two types namely (i) voluntary merger of two units, one of which may be sick, and (ii) compulsory merger of a sick unit with a willing healthy unit. The special legislation should provide for both as merger is a least cost method for revival of a sick unit.
- 11.9 Incidentally, the working group on merger of sick industrial units headed by Shri H. N. Ray in its report of July 1976 made the following recommendations regarding the merger of potentially viable sick units with other units :

"In the interests of employment and production and in order to avoid a heavy drain on the exchequer, it is necessary to explore ways in which potentially viable sick units can be revived through voluntary merger with sound units. Under the existing conditions, not many sound concerns will come forward to take over units which have been languishing for a long period. Hence an environment conducive to voluntary merger of sick units with sound ones has to be created by providing incentives and removing impediments to speedy action. For this a special scheme may be implemented through an enabling legislation to supplement the existing legal provisions regarding merger and reconstruction of companies. For mergers and take-overs coming under the scheme, the following concessions, facilities and relaxations from the regulating provisions of Companies Act, MRTP Act, etc. may be allowed.

(i) Existing provisions of the Companies Act relating to amalgamation of companies will not apply. Approved mergers will be governed by the procedure to be laid down through special legislation.

(ii) In suitable cases, the restrictive provisions of the MRTP Act also will not apply to approved mergers.

(iii) In the event of merger, the benefit of carry-forward and set-off of unabsorbed depreciation and losses of the absorbed company should be allowed to the company absorbing it.

(iv) Such companies should also be given credit by banks and financial institutions on terms consistent with the needs of each merger proposal, and subject to such conditions as the banks and financial institutions may deem necessary. The convertibility clause attaching to loans from financial institutions need not in such cases be insisted upon.

(v) Repayment of liabilities of the sick unit taken over by the absorbing company should be rescheduled. The enabling legislation should provide for a moratorium on the liabilities of the sick units in the event of a merger/take-over approved under the special scheme. Current dues on account of provident fund and other payments to workers should, however, not be delayed.

(vi) A scheme of retirement of surplus workers may be worked out in consultation with the representatives of labour where retrenchment is found to be unavoidable for the economic viability of the concern."

11.10 While the recommendation regarding tax benefit was implemented by amending the Income-tax Act for creation of specified authority under section 72A of the Income-Tax Act and for giving benefit or carry-forward and set-off of unabsorbed depreciation and losses of the absorbed company to the company absorbing it, the suggestion for special legislation for merger has not yet been implemented. The abovementioned recommendations of Ray Committee on merger and surplus labour are being taken care of in the proposed special legislation.

11.11 The special legislation should provide for compulsory and voluntary merger of companies owning sick units with willing healthy companies without going through the procedures of the Companies Act and MRTP Act and also at the same time granting tax benefits through carry-forward of unabsorbed depreciation and business losses now incorporated under sec. 72A of the Income Tax Act. The proposed Board for Industrial Revival (BIR) (which is dealt with later in this Report) may have the same powers as a specified authority, and it may accordingly pass orders in terms of section 72A as well, subject to an amendment that the carry-forward of the whole or a part of the unabsorbed depreciation and business losses may be approved under this legislation depending upon the requirement of funds for revival of the concerned sick unit.

11.12 BIR would also be vested with authority for merger of a healthy unit with a sick unit. If a sick unit takes over a healthy unit, the merged company continues to have the tax benefit of carry forward losses. If the healthy unit takes over a sick unit, then it can get the benefit of the carry-forward losses only under section 72A of the Income Tax Act. Both these formats are identical in ultimate analysis inasmuch as both the companies would get merged and result in a single entity. If a pragmatic view is taken in the ultimate analysis of removing sickness in

the industry, any take-over of sick unit by an industrial unit would enable it to get the benefit of carry-forward losses. This is bound to result in loss of revenue under the Income Tax Act. But the country's ultimate gain could be much larger by reviving these sick units. Even the tax benefit may also diminish inasmuch as the revenue Government gets due to increased production might be much larger than the tax concession given under the Income Tax Act. BIR may also be authorised to approve amalgamation for the purpose of according tax benefit whether the definition of amalgamation given under Income Tax Act is satisfied or not.

11.13 The present section 72A envisages decisions to be taken only by the Central Government on recommendations of the specified authority. However, as suggested by us earlier the decision making power envisaged under that section should rest with the BIR and suitable provisions made in this regard. BIR can also exercise these powers suo moto.

11.14 The Memorandum of Association of some of the companies does not provide for their merger with other companies. Merger proposals, therefore, get delayed as the Memorandum is required to be amended at the general body meeting. To avoid such difficulties, mergers approved under the special legislation should be irrespective of the contents of the Memorandum of companies concerned and should have overriding effect.

11.15 A view was expressed that where a sick unit belongs to an MRTTP group, its amalgamation with another healthy company in the same group should be compulsorily ordered even though the healthy unit may not be willing for such an arrangement. It was mentioned that this may be specially desirable because prosperity of one unit might be partly dependent on the other unit in the group and also because of the need that the persons in the control of the group are made responsible for the overall affairs of the whole group rather than their concentrating on the flourishing unit only. It was however felt that such compulsion may not necessarily result in revival of sick units which is the basic objective of the proposed legislation, and that the better course for the banks and financial institutions would be to persuade the healthy units belonging to MRTTP houses to accept responsibility of the sick units of the same houses by merging them.

Transfer on lease

- 11.16 The method of leasing out has many difficulties under the Income Tax Act. Normally, such a company has much carry-forward losses under the Income Tax Act. When the industrial unit is leased out, the Company gets revenue income by way of rent. Strictly speaking, rent income is different from business income. This rent should be set off against the carry-forward business losses. However, there have been various legal pronouncements on the subject holding both ways viz. in some cases, it can be set off and in some cases, it cannot be set off. It would be desirable to clarify the legal position and to make it abundantly clear that the lease-rent received from an industrial unit would be set off against the loss of the same unit carried forward from earlier years.
- 11.17 The order of BIR for leasing the undertaking of the sick unit should fix the manner of execution of the lease, the terms and conditions of the lease, the amount of the lease-rent and its utilisation for meeting the old liabilities of the unit, etc. On the expiry of the lease (or, as the case may be, the extended lease), BIR may make appropriate arrangements for its efficient working.

Sale as a running concern

- 11.18 The I (D & R) Act has provided for sale of the running concern. However, several difficulties have been encountered in selling units as running concerns. First, the reserve price is fixed by taking into account the financial condition and the liabilities of the concern, etc. Some of these factors are unrelated to the price of the undertaking. The result is that the reserve price fixed on the basis of these factors is likely to be unrealistic. Secondly, under section 18FE(7) of the Act if the reserve price is not forthcoming, the Central Government has to buy the undertaking. Thirdly, unless some satisfactory arrangement is reached between the new purchaser and the labour regarding rationalisation, clearing of the employers' old liability including gratuity, etc., sale does not take place. Fourthly, even though the purchaser may be willing to offer the reserve price, he may not have cash to pay the entire price in one lump sum. In the proposed legislation these difficulties have to be taken care of.
- 11.19 We also suggest that the reserve price should be related to the market price taking into account the value of the assets and the goodwill of the undertaking but not the liabilities. Secondly, if the reserve price is not forthcoming in the first instance, the concerned financial institutions or banks should request BIR to

have it sold by public auction without reference to the reserve price. As for the labour, BIR should have the power to determine the surplus labour as also the kind of liability of labour that would pass on to the purchaser, or would have to be otherwise met. In case of inability of the purchaser to pay the entire amount in cash in one lump sum on the basis of a scheme submitted to it, BIR may allow carry-over of secured liabilities and permit payments by instalments by way of rescheduling the dues of the financial institutions and banks.

Take-over of a sick unit by a healthy unit by purchase of shares

- 11.20 Sale of shares can be approved by BIR only if it is acceptable to both the parties. On application, BIR can approve the sale irrespective of the provisions contained in MRTP Act. BIR may also approve, if it is so satisfied, carry forward of the unabsorbed depreciation and accumulated business losses for a further period of 8 years from the date the scheme comes into effect as recommended by H. N. Ray Committee.

Liquidation of owning company and purchase of its assets

- 11.21 When the financial institutions or banks are satisfied that the sick undertaking is unviable and none of the proposed remedies can revive it, they can propose to BIR liquidation of the undertaking and sale of its assets by public auction. BIR may consider and approve a summary procedure without recourse to the provisions of the Companies Act and distribute the sale proceeds to satisfy the liabilities in a manner to be decided by BIR.

Nodal Agency

- 11.22 We are of the view that the responsibility to prepare a scheme for revival should be cast on the banks, financial institutions or IRCI as a nodal agency. IRCI was set up as a specialised agency to rehabilitate and revive sick and closed industrial units. Over a decade it has built up expertise to diagnose industrial sickness and suggest remedial measures. In view of the foregoing, IRCI is considered fit to act as a Nodal Agency to assist BIR in discharge of its functions. During our deliberations, it was mentioned that this power might be open to challenge if it were delegated to a financial institution (nodal agency) on the ground that the financial institution is itself an interested party. But in our view even if the financial institution is regarded as an interested party, the objection on this ground may not sustain because the scheme is ultimately to be submitted for approval to an independent body,

namely the BIR which would have the power to approve the scheme with or without modifications or rescind it. In this connection, reference may be made to section 45 of the Banking Regulation Act, sections 28 to 30E of the IFC Act, sections 29 to 32F of the SFCs Act, which indicate that powers to deal with a sick unit can be conferred on an authority which may be regarded as an interested party.

- 11.23 We are of the opinion that BIR should be an independent statutory body and should consist of three members — one full time Chairman and two other full time members taken from specialised fields such as finance, accountancy, management, engineering, law, etc. If necessary, BIR can co-opt other members, either for particular cases or generally. As indicated earlier, BIR should be free to adopt a summary procedure for its working and its decision in regard to the manner of revival of a sick unit and other incidental matters should be binding on all concerned parties. To ensure finality and speed, we are of the view that the decision of BIR should be made non-justiciable.
- 11.24 While BIR should be empowered to act suo moto, as suggested earlier, the banks and financial institutions which have granted financial assistance to the unit should first try to rehabilitate it. If the attempts of the institutions and banks at rehabilitation fail, the matter could then be taken up by them to BIR by submitting a proposal for revival. BIR may ask the concerned parties to give their written submission. This suggestion is being made to avoid undue delays which may be caused by continuous oral hearing or arguments. If the scheme contemplates merger of the sick unit, the financial institution or the bank submitting the proposal should simultaneously forward to BIR the consent of the transferee unit. A time frame should be prescribed for completion of formalities at various stages keeping in view the need for speedy revival. Proposals may also be submitted by the Central or State Government. In case of voluntary mergers, the proposals may be submitted by the concerned companies also. BIR may obtain the assistance of IRCI as nodal agency with regard to the consideration of the proposals, etc. received by it.
- 11.25 If BIR decides that a particular unit cannot be revived under the proposed scheme, a copy of its findings should be simultaneously sent to the Government.
- 11.26 If the scheme contemplates take-over of the management or possession of the undertaking, such take-over has necessarily to be related to the other remedies with a view towards the eventual revival of the unit.

11.27 When a proposal for revival is submitted to it, BIR should consider if the following conditions are satisfied :

- (i) The undertaking under reference is sick.
- (ii) The unit should be capable of being revived unless the proposal is for liquidation of the company.
- (iii) If the proposal relates to the reconstruction or change of ownership or management, sale or merger of the company, the new ownership/reconstructed company will be capable of implementing the scheme of revival.
- (iv) Any other condition that may be notified by BIR or the Central Government under the Special Legislation.

During the period such proposal is under its consideration, BIR if it considers necessary, with the assistance of IRCI, can exercise the following powers viz. suspension of onerous or unfair contracts and obligations and stay of legal proceedings relating thereto, appointment of directors and managers.

11.28 The scheme may be sanctioned by BIR with or without modifications within a period normally not exceeding 3 months from the date of receipt of the proposal. In exceptional cases, the BIR may at its option and for reasons to be recorded in writing extend the said period, by another one month. The scheme as sanctioned shall be binding on the sick undertaking, its creditors, members, financial institutions and banks and all other persons or authorities whose rights or interests are involved.

12. Procedure

12.1 While dealing with BIR, procedural aspects have also been suggested. In short, under the proposed special legislation, the BIR should follow the principles of natural justice and also proceed with the matter expeditiously. BIR should follow its own procedures without being influenced by the procedures laid down in other statutes like Civil Procedure Code, etc. BIR will have the powers of a Civil Court in passing orders and in matters relating to execution or enforcement thereof. For the sake of convenience, an indicative draft of the special legislation is annexed to this Report.

13. Competence of Parliament to enact the special legislation

13.1 The industries falling within the Union List in the Seventh Schedule to the Constitution are — (i) the industries declared by

Parliament by law to be necessary for the purpose of defence or for the prosecution of war (Entry 7) and (ii) industries, the control of which by the Union is declared by Parliament by law to be expedient in the public interest (Entry 52). However, the matters pertaining to co-operative societies are within the legislative competence of the State Legislature (Entry 32 of the State List). Therefore, the only manner in which Parliament can legislate in respect of sick industries would be by dealing with sick industrial undertakings (whether they are run or owned by companies, co-operative societies or otherwise) covered by categories of industries specified in the schedule to the legislation. No doubt this might limit coverage of all industries through the proposed enactment. The list mentioned in the schedule to the I (D & R) Act may be adopted for our present purpose. No doubt this list should also be enlarged by inclusion of other process or service industries like hotel, shipping etc. This would require further declaration in terms of Entry 52 in Union List.

14. Legal feasibility of the special legislation

- 14.1 Against the broad outline of the legislative measure indicated above, the next question for consideration is whether a legislation in this form is legally feasible. The doubt about its feasibility can arise on two counts viz., (i) this legislation and/or a scheme as above framed in pursuance of it violates some of the fundamental rights, and (ii) it constitutes circumvention of the principles of natural justice insofar as a financial institution which is a lender of the sick unit has been given the power to submit a proposal ostensibly for its revival whereby it can affect the rights and interests of the undertaking, its creditors, members and third parties.
- 14.2 The objection based on the principles of natural justice can perhaps be met in the manner indicated in paragraph 11.22. As regards the objection regarding constitutional validity, while it can perhaps be established that the measure falls within the categories of excepted legislations provided in Part III (Fundamental Rights) of the Constitution itself or within the exceptions recognised by the Courts, the more advisable course would be to place the legislation under consideration in the Ninth Schedule of the Constitution so that it is free from any challenge on the ground of violation of the fundamental rights. It is true that the Ninth Schedule was intended to cover legislation pertaining to agrarian reforms. But this constraint does not seem to operate now as laws such as FERR Act and I (D & R) Act have also been placed in that Schedule. It would, therefore, seem open to place the proposed legislative measure in the Ninth Schedule.

Alternatively, the special measure, which is designed to control the material resources of the community with a view to saving them from being misused or dissipated, may carry a declaration that it is for giving effect to the policy of the State towards securing the principle specified in clause (b) of Article 39 of the Constitution. Such a declaration would save the special legislation from the above challenge as provided in Article 31C.

15. Conclusion

- 15.1 In conclusion, we would like to state that in examining the need for special legislation to deal with problems of sick units, we have been objectively guided by what may be called the hard experience of banks and financial institutions, as also of the Government in practical application of the relative procedures, howsoever well laid and well intended, under the Companies Act and more particularly I (D & R) Act the inherent limitations of which have led to eventual recourse to nationalisation which course may not be desirable or resorted to in all cases. The various limitations latent in and the inadequacies of the existing legal framework, the role of which so far as rehabilitation of sick units is concerned, is at best incidental within their overall objectives, have been dealt with in the foregoing paragraphs. The need for salvaging productive assets, utilisation of idle installed capacity with the sick units and rescuing large public institutional funds blocked with them, can hardly be over-emphasised. It is felt that the summary procedure contemplated under the proposed special legislation will provide an effective and speedy mechanism for revival of sick industrial units and subserve the larger public interest in the context.

(T. Tiwari), Chairman

(Dr. R. K. Hazari), Member

(Dr. P. D. Ojha), Member

(D. R. Mehta), Member

(S. C. Mittal), Member

(P. K. Ahuja), Member

(Dr. V. K. Agarwal), Member

(Y. V. Sivaramakrishnayya), Member

(R. Viswanathan), Member

(R. Sreekrishnan), Member

(K. L. Roy), Member

(S. A. Naik), Member

(R. Jagannathan), Member

(D. N. Davar), Member

(C. Chandrasekhar), Member

(M. N. Govindaraj), Member-Secretary

APPENDIX — II (Contd.)

**THE SICK INDUSTRIAL UNDERTAKINGS (REVIVAL)
BILL, 1981 (DRAFT)**

**MINISTRY OF LAW, JUSTICE AND COMPANY
AFFAIRS
(Legislative Department)**

New Delhi, the day of , 1903 Saka

**THE SICK INDUSTRIAL UNDERTAKINGS (REVIVAL)
BILL, 1981 (DRAFT)**

An Act to provide for the revival of sick industrial undertakings and for all matters connected therewith or incidental thereto.

Be it enacted by Parliament in the Thirty-second year of the Republic of India as follows :

CHAPTER I

PRELIMINARY

1. (1) This Act may be called the Sick Industrial Undertakings (Revival) Bill, 1981. Short title and commencement

(2) It shall come into force on such date as the Central Government may, by notification, appoint.

2. It is hereby declared that this Act is for giving effect to the policy of the State towards securing the principles specified in Clause (b) of Article 39 of the Constitution of India. Declaration as to the Policy of the State

Explanation :- In this Section, 'State' has the same meaning as in Article 12 of the Constitution of India.

3. In this Act, unless the context otherwise requires, Definitions

- (a) "appointed day" means the date on which this Act comes into force;
- (b) "Board" means the Board for Industrial Revival constituted under Section 4;
- (c) "industrial undertaking" means any industry carried on in one or more factories by any person, authority or Government and includes the owner thereof where the context so requires or admits;
- (d) "industry" means any business, trade, undertaking, manufacture or calling of employers and includes any

calling, service, employment, handicraft or industrial occupation or avocation and includes —

- i) the manufacture, preservation or processing of goods;
- ii) mining and ship building industry;
- iii) the hotel industry;
- iv) the transport of passengers or goods by road, water, or air including lifts and ropeways;
- v) the generation or distribution of electricity or any other form of power;
- vi) the maintenance, repair, testing or servicing of machinery of any description, vehicles, vessels, motor boats, trailers or tractors;
- vii) assembling, repairing or packing any article with the aid of machinery or power;
- viii) the development of any area of land as an industrial estate;
- ix) fishing or providing shore facilities for fishing or maintenance thereof;
- x) providing special or technical knowledge or other services for the promotion of industrial growth;
- xi) the research and development of any process or product in relation to any of the matters aforesaid;
- xii) any other industry as may be notified by the Central Government.

Explanation : The expression 'processing of goods' includes any art or process for producing, preparing or making an article by subjecting any material to a manual, mechanical, chemical, electrical or any other like operation;

- (e) "nodal agency" means the agency constituted under Section 15.
- (f) "notification" means a notification published in the Official Gazette;
- (g) "Owner" in relation to an industrial undertaking means the person who, or the authority which, has the ultimate control over the affairs of the undertaking and includes a company within the meaning of the Companies Act, 1956 (I of 1956) and a Co-operative Society;

- (h) "prescribed" means prescribed by the Rules made under this Act;
- (i) "Public Financial Institutions" means financial institutions referred to in or notified under Section 4A of the Companies Act, 1956;
- (j) "Reserve Bank" means Reserve Bank of India constituted under the Reserve Bank of India Act, 1934;
- (k) "Scheduled Banks" means banks for the time being included in the Second Schedule to the Reserve Bank of India Act, 1934;
- (l) "Sick industrial undertaking" as may be notified by the Central Government from time to time.
- (m) "State Level Institution" means the Financial Corporations, Development Corporations and Investment Corporations constituted or established by the State Governments in their respective States.

CHAPTER II

Board for Industrial Revival

4. (1) The Central Government may, by a notification, constitute a Board called the Board for Industrial Revival. Board for
Industrial
Revival
- (2) The head office of the Board shall be at a place as may be notified by the Central Government.
- (3) The Board shall consist of a full time Chairman and two full time members drawn from specialised fields such as finance, accountancy, management, engineering and law as may be appointed by the Central Government.
- (4) The Board may co-opt one or more members as it may deem fit, either for a particular case or generally.
- (5) The Chairman and the members shall hold office for a term of three years and the person so appointed shall be eligible for reappointment.
- (6) Notwithstanding anything contained herein the Central Government shall have the right to terminate the term of office of the Chairman or the members of the Board at any time before the expiry of the term specified above by giving him notice of not less than 3 months in writing or 3 months salary and allowances in lieu of such notice; and the Chairman or the members of the

Board shall also have the right to relinquish his office at any time before the expiry of the term specified above by giving to the Central Government notice of not less than 3 months in writing.

- (7) The Chairman and the members shall receive such salary and allowances as may be determined by the Central Government.
- (8) The Board shall meet at such times and places as may be notified by the Central Government.
- (9) The functions of the Board shall be as follows :
 - i) to consider and if thought fit to sanction, with or without modification, proposals relating to any sick industrial undertaking for
 - a) change in or take over of management of the sick industrial undertaking;
 - b) reconstruction including restructuring of share capital and liabilities of the sick industrial undertaking;
 - c) merger or amalgamation of two industrial undertakings one of which is a sick industrial undertaking;
 - d) leasing the whole or any part of the sick industrial undertaking;
 - e) sale of the sick industrial undertaking as a running concern;
 - f) take over of a sick industrial undertaking by purchase of shares by any other industrial undertaking;
 - g) liquidation or dissolution of the sick industrial undertaking and if found expedient, purchase of its assets.
 - ii) to attend to such other matters as may be notified by the Central Government.

Effect of
order of
Central
Government

5. No order by the Central Government appointing any person as the Chairman or member of the Board shall be called in question in any manner.

Defects in
appointments
not to invalidate
acts etc.

6. (1) No act or proceeding of the Board shall be questioned on the ground merely of the existence of any vacancy in, or defect in the constitution of the Board.

(2) No act done by any of the Chairman, members or officers or employees of the Board acting in good

faith as such shall be deemed to be invalid merely on the ground that he was disqualified to act as such or that there was any other defect in his appointment.

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|--|--|
| <p>7. The Chairman and the members of the Board shall be indemnified by the Central Government against all losses and expenses which, under the Code of Civil Procedure, 1908, a Civil Court has for the purpose of recovery of the amount due under a decree.</p> | <p>Indemnity of Chairman and members</p> |
| <p>8. (1) The Board shall furnish to the Central Government within four months from the 30th day of June each year a report on its working during the relevant year and the Central Government shall, as soon as may be after they are received by it, cause the same to be laid before each House of Parliament.</p> | <p>Reports</p> |
| <p>(2) The Board shall furnish, from time to time, to the Central Government such returns as the Central Government may require.</p> | <p>Returns</p> |
| <p>9. (1) The Board may appoint such number of officers and employees as it considers necessary or desirable for the efficient performance of its functions and for assisting it in the efficient performance of its functions and determine the terms and conditions of their appointment and service.</p> | <p>Power to appoint Officers</p> |
| <p>(2) Notwithstanding anything contained in any other law or in any agreement, for the time being in force, no member of the staff shall be entitled to claim any compensation for, or in relation to any matter concerning his transfer, appointment and no claim in respect thereof shall be entertained by any Court, Tribunal or other authority.</p> | <p>No claim for compensation.</p> |
| <p>10. The Board may, by a general or special order, authorise any officer or other employee of the Board, subject to such conditions and limitations, if any, as may be specified in the order, to perform such of the administrative functions as it may deem necessary, incidental to the exercise of powers and duties under this Act.</p> | <p>Authorisation for administrative functions.</p> |
| <p>11. The Chairman and every member of the Board shall, before entering upon his duties, make a declaration of fidelity and secrecy in the form set out in the First Schedule to this Act.</p> | <p>Declaration of fidelity and secrecy</p> |

Liquidation of
the Board

12. The Board shall not be abolished save by order of the Central Government and in such manner as it may direct.

Procedures
and powers of
the Board

13. i) The Board shall lay down its own procedure for disposing of the proposals received by it and for the conduct of its business; so however that no order shall be passed or direction issued by the Board without giving an opportunity to the sick industrial undertaking and parties concerned of making their written submissions to the Board.

ii) All decisions of the Board shall be by a simple majority,

iii) The Board shall have the same powers as a civil court under the Code of Civil Procedure 1908, while trying summary suits in respect of the following matters :

a) enforcing the attendance of any person and examining him on oath;

b) requiring the production of documents and material objects; and

c) issuing commissions for the examination of witnesses.

iv) The Board shall be deemed to be a civil court for the purposes of Section 195 and chapter XXVI of the Code of Criminal Procedure, 1973 (2 of 1974) and every proceeding before the Board shall be deemed to be a judicial proceeding within the meaning of Sections 193 and 228 of the Indian Penal Code (45 of 1860) and for the purpose of Section 196 of that Code.

v) The Chairman and the members of the Board shall be deemed to be public servants within the meaning of Section 21 of the Indian Penal Code (45 of 1860).

Power to call
for statement or
information

14. (1) The Board may, at any time after a proposal is received by it, as hereinafter provided, require the sick industrial undertaking or any person owning or associated with it as Chairman, director, officer or employee or any person connected therewith to furnish it, within such time as may be specified in the notice or such further time as the Board may allow, any statement or information relating to such sick industrial undertaking and it shall be

the duty of every such sick industrial undertaking, its Chairman, director, officer, or employee or any such person to comply with such requirements.

- (2) Any person authorised by the Board shall be entitled to enter into and upon any premises of the sick industrial undertaking for the purpose of inspecting the nature and condition of its assets, books of account and other records, registers and papers and to report thereon to the Board within such time as the Board may allow and it shall be the duty of every such sick industrial undertaking and all persons connected therewith to co-operate and assist such person in the discharge of his function.

15. (1) Industrial Reconstruction Corporation of India Ltd. shall be the nodal agency. Nodal Agency
- (2) It shall be the duty of the nodal agency to give all such assistance as may be deemed necessary by the Board in the discharge of its functions under this Act. Duty of the nodal agency to give assistance
- (3) It shall be competent for the nodal agency to take the assistance of the panel of Chartered Accountants and Valuers as may be approved by the Board. Power to seek assistance.

CHAPTER III

CHANGE OR TAKE-OVER OF MANAGEMENT, RECONSTRUCTION, MERGER OR AMALGAMATION, LEASE, SALE, TAKE-OVER OF UNDERTAKING OR LIQUIDATION

16. (1) The Central Government, Reserve Bank, State Governments, the Public Financial Institutions, State level institutions, Scheduled Banks or any other person or authority as may be notified, may submit to the Board a proposal for — Proposal
- (a) change or take-over of management of the sick industrial undertaking;
- (b) reconstruction including restructuring of share capital and liabilities of the sick industrial undertaking;
- (c) merger or amalgamation of two industrial undertakings one of which is a sick industrial undertaking;

- (d) leasing the whole or any part of the sick industrial undertaking;
- (e) sale of the sick industrial undertaking as a running concern;
- (f) take over of a sick industrial undertaking by purchase of shares by any other industrial undertaking;
- (g) liquidation or dissolution of the sick industrial undertaking and wherever considered expedient, purchase of its assets.

- (2) Every proposal other than for liquidation or dissolution shall be accompanied by a viability report prepared in the manner as may be prescribed.
- (3) Every proposal for liquidation or dissolution shall be accompanied by a report prepared in the manner as may be prescribed, showing that the sick industrial undertaking is not likely to be viable.
- (4) Every proposal shall be accompanied by a fee as may be prescribed.
- (5) The Board shall dispose of such proposal within a period not exceeding three months from the date of its receipt. In cases of exceptional nature the Board may for reasons, to be recorded in writing extend the said period by one month.

Board may seek assistance of the nodal agency

- (6) Where such a proposal involves a reconstruction of share capital and liabilities or a merger or lease or sale of a sick industrial undertaking, the Board may, at its discretion, seek the assistance of the nodal agency in the fixation of the reserve price, lease rent or share exchange ratio as the case may be or generally in the formulation of a scheme for the aforesaid purposes.

Power of the nodal agency to call for statement or information

- (7) To assist the Board as aforesaid, it shall be competent for the nodal agency to call upon a sick industrial undertaking to furnish it expeditiously any statement or information relating to or connected with such sick industrial undertaking and it shall be the duty of every such sick industrial undertaking to comply with such requirements.

Inventory

- (8) The nodal agency shall as soon as may be thereafter prepare and cause to be prepared —

- a) a complete inventory of —
- i) all properties, moveable and immoveable, including lands, buildings, works, workshops, stores, instruments, plants, machinery, automobiles and other vehicles, stocks of materials in the course of production, storage or transit, raw materials, cash balances, cash in hand, deposits in bank or with any other person or body or on loan, reserve funds, investments and book debts and all other rights and interests arising out of such property as were in the ownership, possession, power or control of the sick industrial undertaking, whether within or outside India; and all books of account, registers, maps, plans, sections, drawings, records, documents of title or ownership of property and all other documents of whatever nature relating thereto; and
 - ii) all borrowings, liabilities and obligations of whatever kind of the sick industrial undertaking including subsisting liability on account of terminal benefits to its employees.
- b) a list of members, and a list of creditors, of such sick industrial undertaking showing separately in the list of creditors, the secured creditors and the unsecured creditors.
- c) a valuation report in respect of the shares and assets of a sick industrial undertaking in order to arrive at the reserve price for the sale of the sick industrial undertaking as a running concern or for fixation of the lease rent or share exchange ratio.

17. The Board may on receipt of any application or information and on being satisfied that it is a fit case direct the nodal agency to submit an appropriate proposal for its consideration.

Board may
act suo moto

18. During the period the Board is seized of any such proposal or at any time thereafter for the due implementation of the proposal as decided by the Board —

Rationalisa-
tion of labour

- (1) the Board may determine, on the basis of the report of the nodal agency, or otherwise what

complement of labour is necessary for the requirements of the sick industrial undertaking, the extent of and the manner in which labour rationalisation including payment of compensation is to be effected and such other matters incidental thereto.

(2) (a) The Board may declare that —

Suspension
of certain
enactments

(i) all or any of enactments specified in the Second Schedule hereto and the proceedings thereunder shall not apply or shall apply with such adaptation whether by way of modification, addition or omission (which does not, however, affect the policy of the said enactments) to such sick industrial undertaking as may be decided by the Board.

Suspension of
contracts

(ii) the operation of all or any of the contracts, assurances of property, agreements, settlements, awards, standing orders or other instruments in force (to which such sick industrial undertaking is a party or which may be applicable to such sick industrial undertaking) immediately before the date of such proposal, shall remain suspended or that all or any of the rights, privileges, obligation and liabilities accruing or arising thereunder before the said date, shall remain suspended or shall be enforceable with such adaptations and in such manner as may be specified by the Board.

No such declaration shall be made for a period exceeding two years which may be extended by one year at a time so however that the total period shall not exceed five years in the aggregate.

Effect of
Declaration

(b) Any such declaration shall have effect notwithstanding the Memorandum and Articles of Association or Byelaws and notwithstanding anything to the contrary contained in any other law, agreement or instrument or any decree or order of a court, tribunal, officer or other authority or of any submission, settlement or standing order.

Stay of
Proceedings

(c) Any remedy for the enforcement of any right, privilege, obligation and liability referred to above and suspended or modified, and all pro-

ceedings relating thereto pending before any court, tribunal, officer or other authority shall accordingly remain stayed or be continued subject to such adaptations, so however, that on the Board notifying that such declaration shall cease to have effect —

- i) any right, privilege, obligation or liability so remaining suspended or modified, shall become revived and enforceable as if the declaration had never been made;
 - ii) any proceeding so remaining stayed shall be proceeded with, subject to the provisions of any law which may then be in force, from the stage which had been reached when the proceedings became stayed.
- (d) In computing the period of limitation for the enforcement of any right, privilege, obligation or liability, the period during which it or the remedy for the enforcement thereof remains suspended, shall be excluded.
- (3) (a) The Board may appoint whole time or non-whole time directors on the Board of the sick industrial undertaking for such period and on such terms as may be deemed expedient in the circumstances of each case.
- (b) The power to appoint directors under this section includes the power to reappoint and also to appoint any individual to be the manager (by whatever name called) of a sick industrial undertaking.
- (c) Nothing in the Companies Act, 1956, or in any other law for the time being in force, or in the Memorandum, Articles of Association or any other instrument relating to the sick industrial undertaking shall, insofar as it makes in relation to a director, any provision for the holding of any share qualification, age limit, restriction on the number of directorships, retirement by rotation or removal from office, apply to any director appointed under this section
- (d) Any director appointed as aforesaid shall :-
- i) hold office for such period as may be specified by the Board and may be removed

Extension of
period of
limitation

Board's right
to appoint
Directors and
its operation.

- or substituted by any person by order in writing of the Board;
- ii) not incur any obligation or liability by reason only of his being a director or for anything done or omitted to be done in good faith in the discharge of his duties as a director or anything in relation thereto;
 - iii) not be liable to retirement by rotation and shall not be taken into account either in the number of directors which the sick industrial undertaking may have or for computing the number of directors liable to retirement.
- (e) Every such director shall be indemnified by the sick industrial undertaking against all loss and expenses incurred by him in or in relation to the discharge of his duties except such which are caused by his own wilful act or default.
- (f) Such director shall not be responsible for any other director or for any officer or other employee of the sick industrial undertaking or for any loss or expenses resulting to the sick industrial undertaking from the insufficiency or deficiency of the value of, or title to any property or security acquired or taken on behalf of the sick industrial undertaking or the insolvency or wrongful act of any debtor or any person under obligation to the sick industrial undertaking or anything done in good faith in the execution of the duties of his office in or in relation thereto.
- (g) No suit or other legal proceeding shall lie against the Board or any director appointed by it or any other person authorised by the Board to discharge any functions under this Act for any loss or damage caused or likely to be caused by anything which is in good faith done or omitted to be done in pursuance of this Act or any other law or provision having the force of law.

Offences to be referred to appropriate authority.

19. Where on the basis of available material the Board is of the opinion or has reason to believe that an offence punishable under any law has been committed by any per-

son who has taken part in the promotion, formation or management of the sick industrial undertaking or by any director, manager or officer thereof, the Board may issue suitable directions for filing of complaint before the appropriate authority.

20. Notwithstanding anything to the contrary contained in the Indian Limitation Act, 1963, or in any other law for the time being in force relating to limitation there shall be no period of limitation for the recovery of arrears of calls from any promoter, director, officer or manager of a sick industrial undertaking or for the enforcement by the sick industrial undertaking against any of its promoters, directors, officers, managers or shareholders of any claim based on a contract, expressed or implied; and in respect of all other claims by the sick industrial undertaking against its promoters, directors, officers, managers or shareholders the period of limitation shall be six years from the date of submitting of the proposal under section 16.

Limitation for recovery of arrears of calls etc.

21. (1) If, in the course of scrutinising any such proposal, as is referred to in section 16, it appears to the Board that any person who has taken part in the promotion, formation or management of the sick industrial undertaking, including any past or present director, manager or officer of the sick industrial undertaking

Misfeasance proceedings.

(a) has misapplied or retained, or become liable or accountable for, any money or property of the sick industrial undertaking; or

(b) has been guilty of any misfeasance, malfeasance or nonfeasance or breach of trust in relation to the sick industrial undertaking,

the Board may direct him to repay or restore the money or property or any part thereof, with or without interest, as the Board thinks just, or to contribute such sum to the assets of the sick industrial undertaking, by way of compensation in respect of the misapplication, retention, misfeasance, malfeasance, nonfeasance or breach of trust, as the Board thinks just.

(2) The Board may examine any person or document as it considers necessary for the aforesaid purpose.

- (3) Any person having in his possession relevant material or knowledge thereof shall have a right to appear before the Board, with a written submission, in order to prove or disprove any of the aforesaid allegations.
- (4) No such direction shall be given by the Board under this section unless such person has been given an opportunity of being heard by means of written submissions.
- (5) Where such a direction is given jointly against two or more such persons, they shall be jointly and severally liable to make the repayment or restoration of the money or property or to contribute by way of compensation.
- (6) Where the Board has reason to believe that a property belongs to any promoter, director, manager or officer of the sick industrial undertaking, or of the sick industrial undertaking itself and such property stands in the name of such person or any other person as an ostensible owner, or is in the possession of such person or any other person, then the Board may, at any time, after making a direction under this section order the attachment and sale of such property or such portion thereof, as it thinks fit and the provisions of the Code of Civil Procedure, 1908 relating to attachment and sale of property shall, as far as may be, apply.
- (7) Every director or other officer of a sick industrial undertaking shall give such assistance to the Board as it may reasonably require in connection with the realisation, restoration and distribution of the sick industrial undertaking.

Attachment
and sale of
property

Avoidance of
certain
transfers

22. Any transfer of property, moveable or immovable, or any delivery of goods made by or on behalf of the sick industrial undertaking not being a transfer or delivery made in the ordinary course of its business or in favour of the purchaser or encumbrancer in good faith and for valuable consideration.

- (i) if made within a period of six months before the submission of the proposal under section 16 shall be void, if it is so declared by the Board;

- (ii) if made during the period the Board is seized of any such proposal, shall be void unless prior approval of the Board is obtained.

23. (1) The Board or the nodal agency on being directed by the Board may in order to take into custody or under its control all property, effects and actionable claims to which a sick industrial undertaking is or appears to be entitled, request in writing, the Chief Metropolitan Magistrate or the District Magistrate within whose jurisdiction any property, books of account or any other documents of such sick industrial undertaking be situate or be found, to take possession thereof, and the Chief Metropolitan Magistrate or the District Magistrate, as the case may be, shall, on such request being made to him —

Power to seek the assistance of Chief Metropolitan Magistrate and District Magistrate.

- i) take possession of such property, books of account or other document; and
- ii) forward them to the Board or the nodal agency.

(2) For the purpose of securing compliance with the provisions of sub-section (1), the Chief Metropolitan Magistrate or the District Magistrate may take or cause to be taken such steps and use or cause to be used such force as may, in his opinion, be necessary.

(3) No act of the Chief Metropolitan Magistrate or the District Magistrate done in pursuance of this section shall be called in question in any Court or before any authority on any ground whatsoever.

24. (1) Where the Board is satisfied that the affairs of the sick industrial undertaking can be better managed with the change or the take-over of the existing management of the sick industrial undertaking, pending consideration of any proposal for revival of such sick industrial undertaking or thereafter, the Board may direct —

Change or take over of management.

- (i) the removal of any of the directors or other personnel from their posts as in the opinion of the Board seems fit;
- (ii) the appointment of directors or other personnel in the resulting vacancies caused by

such removal by induction of persons at appropriate levels;

- (iii) the appointment of additional directors and personnel in the sick industrial undertaking; or
- (iv) the replacement of all the directors of the sick industrial undertaking by new directors;
- (v) the appointment of an authorised person to manage the sick industrial undertaking which belongs to an owner having more than one industrial undertaking.

(~~Explanation~~ : The authorised person may be an individual or a body of individuals, a firm or a company, and shall be deemed to be capable of suing and being used in such name).

- (2) The Board may also direct the manner in which and the other terms and conditions on which such appointment or appointments shall take effect.
- (3) Such appointments shall be for a period not exceeding three years initially, which may, in suitable cases, be extended by a period of one year at a time as the Board may think just.
- (4) Such direction shall take effect notwithstanding the Memorandum and Articles of Association or Byelaws and notwithstanding anything to the contrary contained in any law, agreement or instrument or any decree or order of a court, Tribunal, Officer or other authority or of any submission, settlement or standing order.
- (5) On the issue of a direction by the Board as aforesaid —
 - (a) all persons holding such posts immediately before the issue of such direction, shall be deemed to have vacated their offices as such;
 - (b) any contract between the sick industrial undertaking and any such persons holding office as such immediately before the issue of such direction shall be deemed to have been terminated;
 - (c) the Board of Directors as so reconstituted or the authorised person as the case may be, shall take all such steps as may be necessary

for the purpose of efficiently managing the business of the sick industrial undertaking and shall exercise all such duties as may be specified in the direction given by the Board and shall also take all such steps as may be necessary to take into their custody or control all the property, effects and actionable claims to which the sick industrial undertaking is or appears to be entitled and all the property and effects of the sick industrial undertaking shall be deemed to be in the custody or control of the Board of Directors as so reconstituted or the authorised person, as the case may be, as from the date of such direction and they may approach the Board for assistance, if necessary, in terms of section 23.

- (d) the Board of Directors as so reconstituted or the authorised person, as the case may be, shall alone be entitled to exercise all the powers of the directors of the sick industrial undertaking, whether such powers are derived from the Companies Act, 1956 or from the Memorandum or Articles of Association or Byelaws of the sick industrial undertaking or from any other source.
- (6) No person who ceases to hold any office or whose contract is terminated by reason of the provisions of this section shall be entitled to any compensation for the loss of office or for the premature termination of his contract provided that nothing contained in this section shall affect the right of any such person to recover from the sick industrial undertaking monies recoverable otherwise than by way of such compensation.
- (7) i) The Board may give such further directions as it may consider necessary for the proper and efficient management of the sick industrial undertaking by the Board of Directors as so reconstituted or by the authorised person including the maintenance of accounts, books and records.
- ii) The Board may also give directions in respect of the financial requirements of the sick in-

dustrial undertakings, the manner in which such funds may be secured and such other matters as are incidental thereto.

Reconstruction
of the share
capital and
liabilities of
the sick in-
dustrial under-
taking.

25. (1) Where the Board is satisfied that it is desirable to prevent the sick industrial undertaking from going into liquidation by considering a reconstruction (including restructuring of the share capital and liabilities) of the sick industrial undertaking, the Board may cause to be prepared a scheme for reconstruction and may direct that the scheme be prepared if need be with the assistance of the nodal agency and may contain provisions for all or any of the following matters :

- (a) a reasonable capital base, debt equity ratio consistent with the expected return on reconstruction, assets, powers, rights, interests authorities and privileges, liabilities, duties and obligations of the sick industrial undertaking on its reconstruction;
- (b) the issue of shares at discount or special share capital, to all or any of the public financial institutions or their nominees carrying special rights in respect of voting and as to payment of dividend and return of capital;
- (c) the transfer of such shares or of the special share capital or any part thereof by the public financial institutions to any person to enable them to provide the requisite management;
- (d) the redemption of the special share capital at such point of time as may be specified;
- (e) the conversion, notwithstanding anything to the contrary contained in the Companies Act, 1956 or the Capital Issues Control Act, 1941, read with the Capital Issues (Exemption) Order, 1969, of the whole or any portion of the outstanding loans/debentures of the public financial institutions and banks into equity or special share capital, as the case may be, either at par or at such discount as may be approved by the Board, of the sick industrial undertaking on its reconstruction;
- (f) the alteration of the Memorandum and Articles of Association or Byelaws of the sick in-

dustrial undertaking, to give effect to such reconstruction;

- (g) subject to the provisions of the scheme of reconstruction, the continuation by, or against the sick industrial undertaking, on its reconstruction of any action or proceeding pending against the sick industrial undertaking immediately before the date of its reconstruction;
- (h) the reduction of the interest or rights which the members and creditors have in or against the sick industrial undertaking before its reconstruction to such extent as the Board may consider necessary in the interest of the general public or in the interest of the members and creditors or for the maintenance of the business of the sick industrial undertaking;
- (i) the payment in cash or otherwise to the creditors in full satisfaction of their claim —
 - i) in respect of their interest or rights in or against the sick industrial undertaking before its reconstruction; or
 - ii) where their interest or rights in or against the sick industrial undertaking has or have been reduced under Clause (h) above in respect of such interest or rights as so reduced;
- (j) the allotment to the members of the sick industrial undertaking for shares held by them therein before its reconstruction whether their interest in such shares has been reduced under Clause (h) or not, of shares in the sick industrial undertaking on its reconstruction and where it is not, possible to allot shares to any members, the payment in cash to those members in full satisfaction of their claim :-
 - i) in respect of their interest in shares in the sick industrial undertaking before its reconstruction;
 - ii) where such interest has been reduced under Clause (h) above, in respect of their interest in shares as so reduced;

- (k) the offer by the Central Government to acquire by negotiation with the members of the sick industrial undertaking their respective shares on payment in cash to those members who may volunteer to sell their shares to the Central Government in full satisfaction of their claim —
 - i) in respect of their interest in shares in the sick industrial undertaking before its reconstruction; or
 - ii) where such interest has been reduced in Clause (h) above in respect of their interest in shares so reduced;
- (l) the conversion of any loans or debentures into equity or special share capital including shares at discount of the sick industrial undertaking after the reconstruction and the allotment of those shares to such creditors or debentureholders, as the case may be;
- (m) the increase of the share capital of the sick industrial undertaking by the issue of new shares or special shares or shares at discount and the allotment of such new shares or special shares or shares;
- (n) the continuance of the services of such of the employees of the sick industrial undertaking as the Board may specify in the scheme of reconstruction in the sick industrial undertaking itself, on its reconstruction, on such terms and conditions as the Board thinks fit;
- (o) notwithstanding anything contained in clause (n) above, where any employee of the sick industrial undertaking whose services have been continued under Clause (n) above, has, by notice in writing given to the sick industrial undertaking at any time before the expiry of one month next following the date on which the scheme of reconstruction is sanctioned by the Board, intimated his intention of not becoming an employee of the sick industrial undertaking, on its reconstruction, the payment to such employee and to other employees, whose services have not been continued on the reconstruction of the sick in-

dustrial undertaking, of compensation, if any, to which they are entitled under the Industrial Disputes Act, 1947 (14 of 1947) and such pension, gratuity, provident fund and other retirement benefits ordinarily admissible to them under the rules or authorisations of the sick industrial undertaking immediately before the date of its reconstruction;

- (p) any other terms and conditions for the reconstruction of the sick industrial undertaking;
 - (q) such incidental, consequential and supplemental matters as are necessary to secure that the reconstruction of the sick industrial undertaking shall be fully and effectively carried out.
- (2) A Scheme shall accordingly be prepared and submitted to the Board for its sanction.
- (3) a) A copy of the scheme, shall be sent in draft form to the members and creditors of the sick industrial undertaking for making written representations within a period to be specified by the Board and the Board shall after considering the representations, if any, received from the members and creditors make such modifications or changes in the draft as it may seem to the Board desirable and necessary and sanction the scheme;
- b) The scheme as so sanctioned by the Board shall come into force on such date as the Board may specify in this behalf; provided that different dates may be specified for different provisions of the scheme.
- (4) Notwithstanding the Memorandum and Articles of Association or Byelaws and notwithstanding anything to the contrary contained in any law, agreement or instrument or any decree or order of a Court, Tribunal, officer or other authority or of any submission, settlement or standing order, the sanction accorded by the Board under the above sub-section shall be final and be conclusive evidence that all the requirements of this section relating to the reconstruction of share capital and liabilities of the sick industrial undertaking

have been complied with, and a copy of the sanctioned scheme certified to be true copy thereof by the Board, shall, in all legal proceedings (whether original or appeal or otherwise) be admitted as evidence to the same extent as the original scheme;

- (5) On and from the date of the coming into operation of the scheme or any provision thereof, the same shall be binding on the sick industrial undertaking and also on all the members and other creditors of the sick industrial undertaking and on any other person having any right or liability in relation to the sick industrial undertaking;
- (6) The provisions of this section and of any scheme made thereunder shall have effect notwithstanding the Memorandum and Articles of Association or Byelaws of the sick industrial undertaking and notwithstanding anything contained in the Companies Act, 1956 (1 of 1956) and Monopolies and Restrictive Trade Practices Act, 1969 (54 of 1969) and Foreign Exchange Regulation Act, 1973 (46 of 1973).

Merger of
sick industrial
undertakings.

26. (1) Where the proposal is for —

- i) a voluntary merger of two industrial undertakings, one of which is a sick industrial undertaking; or
- ii) a compulsory merger of a sick industrial undertaking with another willing industrial undertaking; or
- iii) the merger of a willing industrial undertaking with a sick industrial undertaking;

the Board may cause to be prepared a scheme of merger or amalgamation and may direct that the scheme be prepared with the assistance of the nodal agency which will provide for their merger or amalgamation into a single company with such property, powers, rights, interest, authorities and privileges and with such liabilities, duties and obligations as may be specified by the Board.

- (2) A Scheme of merger and amalgamation shall accordingly be prepared and submitted to the Board for its sanction.

- (3) The Board may make such consequential, incidental and supplemental provisions as may, in its opinion, be necessary to give effect to such merger of amalgamation.
- (4) Notwithstanding anything to the contrary contained in the Income Tax Act, 1961, or under any other tax law for the time being in force, the benefits of carry-forward of accumulated losses and unabsorbed depreciation as provided in section 72-A of the Income-Tax Act, 1961, shall be applicable and available to the industrial undertaking resulting from the amalgamation, and the Board shall for the purpose of this section, be the specified authority and it shall pass orders accordingly on its own motion without the need of following the procedure prescribed thereunder.
- (5) The Board shall cause a copy of the amalgamation proposal to be sent in draft form to each of the amalgamating companies, its members and creditors for making written representations within a period as may be specified by the Board.
- (6) The Board shall, after considering the representations, if any, received from the members, and creditors, make such modifications or changes in the draft as it may seem to the Board desirable and necessary and sanction the scheme.
- (7) Notwithstanding the Memorandum and Articles of Association or the Byelaws and notwithstanding anything to the contrary contained in any law, agreement or instrument or any decree or order of a court, Tribunal, Officer or other authority or of any submission, settlement or standing order, the sanction accorded by the Board under the above sub-section shall be final and be conclusive evidence that all the requirements of this section relating to the amalgamation of the sick industrial undertaking have been complied with, and a copy of the sanctioned scheme certified to be true copy thereof by the Board, shall, in all legal proceedings (whether original or in appeal or otherwise) be admitted as evidence to the same extent as the original scheme.
- (8) On and from the date of coming into operation of the scheme or any provision thereof, the same

shall be binding on both the amalgamating companies, the members and creditors of the industrial undertakings and on any other person having any right or liability in relation to such industrial undertakings.

- (9) The provisions of this section and of any scheme of amalgamation made thereunder shall have effect notwithstanding the Memorandum and Articles of Association or the Byelaws of any sick industrial undertaking and notwithstanding anything contained in the Companies Act, 1956 (1 of 1956), Monopolies and Restrictive Trade Practices Act, 1969 (54 of 1969) and Foreign Exchange Regulation Act, 1973 (46 of 1973).

Leasing of sick
industrial
undertaking.

27. (1) Where the Board is satisfied considering the circumstances of the sick industrial undertaking that it is desirable to give it on lease it may direct that the sick industrial undertaking be given on lease initially for a period not exceeding five years to a willing industrial undertaking on such terms and conditions as may be deemed appropriate by the Board.
- (2) On the issue of a direction by the Board as aforesaid :
- (a) all persons in charge of management including persons holding office as managers or directors of the sick industrial undertaking immediately before the issue of such direction, shall be deemed to have vacated their offices as such;
 - (b) any contract of management between the sick industrial undertaking and manager or director thereof holding office as such immediately before the issue of such direction shall be deemed to have been terminated;
 - (c) the lessee shall take all such steps as may be necessary for the purpose of efficiently managing the business of the sick industrial undertaking and shall exercise all such powers and have all such duties as may be specified in the direction given by the Board and shall also take all such steps as may be necessary to take into his custody or control

all the property, effects and actionable claims to which the sick industrial undertaking is or appears to be entitled and all the property and effects of the sick industrial undertaking shall be deemed to be in the custody or control of the lessee as from the date of such direction and the lessee may approach the Board for assistance, if necessary, in terms of Section 23.

- (d) the lessee shall alone be entitled to exercise all the powers of management of the sick industrial undertaking notwithstanding the Memorandum and Articles of Association or Byelaws of the sick industrial undertaking or anything contained in the Companies Act, 1956 or any other applicable law.
- (3) No person who ceases to hold any office or whose contract of management with the sick industrial undertaking is terminated by reason of the provisions of this section shall be entitled to any compensation for the loss of office or for the premature termination of his contract otherwise than as provided in the lease arrangement. Provided further that nothing contained in this section shall affect the right of any such person to recover from the sick industrial undertaking monies recoverable otherwise than by way of such compensation.
- (4) The Board may fix the lease rent in consultation with the lessee having regard to the existing liability of the sick industrial undertaking its profitability and all other relevant factors and thereafter authorise such lease and make such consequential, incidental and supplemental provisions as may, in its opinion, be necessary to give effect to such lease arrangement.
- (5) The certificate issued by the Board in respect of such lease arrangement shall constitute a document of lease and the provisions of the Transfer of Property Act, 1882 (4 of 1882) and the Indian Registration Act, 1908 (16 of 1908) in relation to leases shall not apply.
- (6) The Board shall direct
 - 1) that the sick industrial undertaking shall be solely liable and responsible for or in respect

of all liabilities and/or obligations incurred or undertaken by the sick industrial undertaking prior to the date of such lease and to agree to indemnify and keep indemnified the lessee from and against all claims, demands, actions or proceedings and all costs, charges, expenses, loss or damage suffered or incurred by the lessee in respect thereof;

- ii) that the lessee shall be solely liable and responsible for or in respect of all liabilities or obligations incurred or undertaken by the lessee during the period of the lease and that the sick industrial undertaking shall in no event, be liable or responsible therefor, and that the lessee shall agree to indemnify and keep indemnified the sick industrial undertaking from and against all claims, demands, actions or proceedings and all costs, charges, expenses, loss or damage suffered or incurred by the sick industrial undertaking in respect thereof or for the maintenance, upkeep and preservation of the assets of the sick industrial undertaking, normal wear and tear excepted.
- (7) The lessee shall be entitled to do or cause to be done all things reasonable and necessary for the efficient and proper conduct of the business of the sick industrial undertaking and to take such steps for filing within time with the concerned Registrar of Assurances, Registrar of Companies and the Registrar of Co-operative Societies, as the case may be appropriate returns in respect of such lease.
 - (8) The lease rent fixed by the Board shall be in accordance with the direction given by the Board so however that such percentage of the rent receipts as to the Board may seem fair and reasonable shall be utilised towards the discharge of the liabilities of the sick industrial undertaking to the public financial institutions and scheduled banks.
 - (9) The Board shall be entitled to extend the period of the lease for such term or terms as it may, in its opinion, deem necessary.

- (10) On the expiry of the lease term (or as the case may be the extended term), the Board may either order the retransfer of the industrial undertaking to its owners or order adoption of such other remedies as may, in the opinion of the Board, be necessary for the smooth running of such undertaking.
28. (1) Where the Board is satisfied that it is desirable to sell the sick industrial undertaking as a running concern, it may cause to be prepared a valuation report to arrive at the fair market value of the assets including good will and may direct that the same be prepared by the nodal agency having regard to :
- (a) the financial condition of the sick industrial undertaking as disclosed in its books of account;
 - (b) the condition and nature of the plant, machinery, instruments and other equipment;
 - (c) the total amount of liabilities on account of terminal benefits to the employees and other borrowings, and other liabilities of the sick industrial undertaking; and
 - (d) other relevant factors including the factor that the sick industrial undertaking will be sold free from all encumbrances or with such encumbrances as may be determined by the Board.
- (2) The valuation report indicating the reserve price shall accordingly be prepared by the nodal agency and submitted to the Board for its determination.
- (3) The Board shall thereafter order the sale of the sick industrial undertaking as a running concern by public auction in such manner as may be determined by it;
- (4) Notwithstanding the Memorandum and Articles of Association or the Byelaws and notwithstanding anything to the contrary contained in any law, agreement or instrument or any decree or order

or a court, Tribunal, Officer or other authority or of any submission, settlement or standing order :

- a) the sick industrial undertaking shall be sold as a running concern, to the highest bidder only if the price offered by him therefor is not less than the reserve price;
 - b) Where there is no offer or price offered is not equal to, or more than, the reserve price, then the Board shall order the sale of the sick industrial undertaking by public auction a second time and if at such auction also the price offered is not equal to, or more than the reserve price, the Board may, in its discretion, sell the sick industrial undertaking at the highest offer received.
- (5) A sick industrial undertaking may be sold free from all encumbrances, or subject to such encumbrances as may be decided by the Board.
 - (6) The sale price shall be paid to the Board in one lump sum or in such instalments as may be determined by the Board.
 - (7) The Board shall take or cause to be taken such steps as may be necessary to recover from the members of the sick industrial undertaking all arrears in respect of calls on the shares made by the sick industrial undertaking or to make calls in respect of the amounts still payable in respect of the shares of the sick industrial undertaking as also to take steps for recovering the debts due to the sick industrial undertaking.
 - (8) Out of the amount so received by the Board together with any other sum which may be realised from the members, debtors or any other person from whom money is due to the sick industrial undertaking, the Board shall order distribution of a fixed percentage pro rata for the discharge of secured liabilities of the sick industrial undertaking and the balance, pro rata for the discharge of unsecured liabilities including compensation to workmen, statutory liabilities, depositors and members of the sick industrial undertaking.
 - (9) Notwithstanding the Memorandum and Articles of Association or the Byelaws and notwithstanding

anything to the contrary contained in any law, agreement or instrument or any decree or order of a Court, Tribunal, Officer or other authority or of any submission, settlement or standing order, the order of sale and the distribution made by the Board shall be final and be conclusive, and shall not be called in question on the ground that it affects the priorities of the liabilities inter se of the sick industrial undertaking.

- (10) The sale ordered by the Board under this section shall be final and be conclusive evidence that all the requirements of this section relating to the sale of the sick industrial undertaking have been complied with, and a copy thereof by the Board, shall, in all legal proceedings (whether original or in appeal or otherwise) be admitted as evidence to the same extent as the original order. Such certificate of sale shall constitute a document of title to the purchaser and the provisions of the Transfer of Property Act, 1882, (4 of 1882), and the Indian Registration Act, 1908 (16 of 1908) shall not apply.
 - (11) On and from the date of the sale, the same shall be binding on the sick industrial undertaking its members, creditors and on any other person having any right or liability in relation to such industrial undertaking.
 - (12) The purchaser shall take such steps for filing within time with the concerned Registrar of Assurances, Registrar of Companies and the Registrar of Co-operative Societies, as the case may be, appropriate returns in respect of such sale.
29. (1) Where a proposal is received by the Board for take-over by purchase of the shares of a sick industrial undertaking (hereinafter referred to as "the Transferor Company"), the Board may cause to be prepared a Scheme or Contract involving the transfer of a majority of the shares or any class of shares in the sick industrial undertaking to another Company (hereinafter referred to as "the Transferee Company) and may direct that the Scheme or Contract be prepared if need be by or with the assistance of the nodal agency.

- (2) The Board shall cause a notice to be issued by the Transferee Company to the shareholders of the Transferor Company of the desire of the Transferee Company to acquire within specified period the shares of the Transferor Company at a share exchange ratio based on the valuation of shares made by the nodal agency.
- (3) The following provisions shall apply in relation to every such scheme or contract, namely :
 - (a) every such offer shall be communicated to all the shareholders of the Transferor Company and shall be accompanied by a recommendation to the shareholders of the Transferor Company by its Directors to accept such offer;
 - (b) every such offer shall contain a statement by or on behalf of the Transferee Company disclosing the steps it has taken to ensure that necessary cash will be available and the period within which the purchase transaction would be put into effect;
 - (c) every such offer shall contain a statement that the Transferee Company shall buy the shares of the dissenting shareholders of the Transferor Company on the same terms as the Transferee Company would be buying the shares of the approving shareholders.
- (4) On the expiry of the period mentioned in the notice, the Board shall, on being satisfied that all the formalities as mentioned above have been complied with by the Transferee Company, order that the shares of the Transferor Company be transferred in the name of Transferee Company, which order shall be binding on all the shareholders of the Transferor Company, including the dissenting shareholders.
- (5) The Board shall, thereafter, cause the instruments of transfer to be executed on behalf of the shareholders of the Transferor Company including the dissenting shareholders to be lodged with it within a period of one month therefrom.
- (6) On the Transferee Company paying or transferring to the Transferor Company the amount or consideration representing the price payable by

the Transferee Company for the shares, the Board shall sanction the scheme or approve the contract whereupon the Transferor Company shall register the Transferee Company as the holder of those shares.

- (7) Any sum or other consideration received by the Transferor Company under this section shall be paid into a separate bank account and any such sums and any other consideration so received shall be held by the Transferor Company in trust for the persons entitled to the shares in respect of which the said sums or other consideration were respectively received.
 - (8) The above provisions shall have effect notwithstanding the Memorandum and Articles of Association or Byelaws of the Transferor Company and the Transferee Company and notwithstanding anything to the contrary contained in the Companies Act, 1956, (1 of 1956), Monopolies and Restrictive Trade Practices Act (54 of 1969), and Foreign Exchange Regulation Act, 1973 (46 of 1973) or any other law for the time being in force.
30. (1) Where the Board has reason to believe, after considering the report submitted to it in terms of sub-section(3) of section 16, that there is no scope of reviving the sick industrial undertaking, it shall order the sale of the assets of the sick industrial undertaking by public auction, and direct the nodal agency to take necessary steps therefor and to apply to the High Court having jurisdiction for the winding up of the sick industrial undertaking.
- Liquidation of the sick industrial undertaking and purchase of its assets
- (2) Such direction of the Board shall be deemed in the case of the Company to be a ground specified in section 433 of the Companies Act, 1956 in which the Company may be wound up by the High Court.
 - (3) The nodal agency shall, as soon as may be, after an order is passed by the Board under sub-section(1) prepare or cause to be prepared a valuation report in respect of the assets of the sick industrial undertaking and submit such reports to the Board for determination of the price.

- (4) Thereafter with the permission of the Board, the nodal agency shall invite tenders from the public in such manner as may be determined by the Board for the sale of the assets of the sick industrial undertaking.
- (5) Notwithstanding the Memorandum and Articles of Association or the Byelaws and notwithstanding anything to the contrary contained in any law, agreement or instrument or any decree or order of the Court, Tribunal, officer or other authority or of any submission, settlement or standing order :
 - i) the assets of the sick industrial undertaking shall be sold to the highest bidder only if the price agreed therefor is not less than the price determined by the Board.
 - ii) where there is no offer or the price offered is not equal to or more than the price determined by the Board, then the Board shall order the sale of the assets of the sick industrial undertaking by public auction a second time and if at such auction also, the price offered is not equal to or more than the price determined by the Board, the Board may in its discretion sell the assets of the sick industrial undertaking at the highest offer received.
- (6) The sale price shall be paid to the Board in one lump sum or in such instalments as may be determined by the Board.
- (7) Out of the amount so received by the Board together with any other sum which may be realised from the members, debtors or any other person from whom money is due to the sick industrial undertaking the Board shall order distribution of a fixed percentage pro rata for the discharge of secured liabilities of the sick industrial undertaking and the balance, pro rata for the discharge of unsecured liabilities including compensation to workmen statutory liabilities, depositors and members of the sick industrial undertaking.
- (8) Notwithstanding the Memorandum and Articles of Association or the Byelaws and notwithstanding anything to the contrary contained in any

law, agreement or instrument or any decree or order of a Court, Tribunal, Officer or other authority or of any submission, settlement or standing order, the sale ordered by the Board and the distribution made by the Board shall be final and be conclusive, and shall not be called in question on the ground that it affects the priorities of the liabilities inter se of the sick industrial undertaking.

- (9) On and from the date of the sale, the same shall be binding on the sick industrial undertaking, its members, creditors and on any other person having any right or liability in relation to such sick industrial undertaking.
- (10) The purchaser shall take such steps for filing within time with the concerned Registrar of Assurances, Registrar of Companies and Registrar of Co-operative Societies, as the case may be, appropriate returns in respect of such sale.
- (11) On the sale of such assets, the nodal agency shall, pursuant to the direction given by the Board under sub-section (1), apply :
 - i) in the case of a company governed by the Companies Act, 1956 to the High Court having jurisdiction for the winding up of the sick industrial undertaking;
 - ii) in the case of a Co-operative Society to the concerned Registrar of Co-operative Societies for dissolution of the Society.
- (12) i) On receipt of such application from the nodal agency under sub-clause (i) of the preceding sub-section, the High Court shall forthwith order the winding up of the sick industrial undertaking and the nodal agency or any other person as may be notified by the Central Government in this behalf shall be the official liquidator of the company owning the sick industrial undertaking and shall take such steps as may be appropriate for the dissolution of the company owning the sick industrial undertaking;
- ii) On receipt of such application from the nodal agency under sub-clause (ii) of the preceding

sub-section, the concerned Registrar shall take such steps forthwith for the dissolution of the Co-operative Society or the Society owning the sick industrial undertaking.

- (13) The order of the High Court under Clause (i) of the preceding sub-section and the action of the Registrar of Co-operative Societies under Clause (ii) of the preceding sub-section shall be final and binding on the sick industrial undertaking, its owners, directors, managers, officers and any other person having any right or liability in relation to such industrial undertaking and shall not be called in question in any manner.

Board to
issue certificate.

31. (1) After the Board has decided to adopt one or more of the modes as referred to in sections 24 to 30, the Board shall after receiving the written submissions from the parties concerned and after considering the same, if it may so decide, issue a Certificate as may be prescribed specifying clearly the reliefs granted and the names and descriptions of the parties against whom such reliefs have been granted, the amount of costs awarded and by whom, and out of what funds and in what proportions, such costs are to be paid and every such Certificate shall be deemed to be a certified copy of the decree for all purposes including execution.
- (2) Any such Certificate issued by the Board shall be conclusive evidence that all the requirements of this Chapter have been duly complied with and shall have effect notwithstanding anything to the contrary contained in any other provisions of this Act or in any other law or any decree, order, agreement, award or other instrument for the time being in force.
- (3) Any such Certificate may be enforced in the same manner in which decrees of the Court made in any suit pending therein may be enforced.
- (4) Notwithstanding anything to the contrary contained in the Code of Civil Procedure, 1902, any person authorised by the Board may apply for the execution of a decree on production of a Certificate issued under this section and on the Board

certifying in writing the amount remaining due or relief remaining unenforced under such Certificate.

- (5) Without prejudice to the provisions of sub-sections (2) or (3), any amount found due to the sick industrial undertaking may be recovered in the same manner as an arrear of land revenue and for the purpose of such recovery, the person authorised by the Board may forward to the Collector, within whose jurisdiction the property of the person against whom any order or decision of the Board has been made is situate, a Certificate, as may be prescribed, issued by the Board specifying the amount so due and person by whom it is payable.
- (6) On receipt of a Certificate under sub-section (5), the Collector shall proceed to recover from such person the amount specified therein as if it were a arrear of land revenue : Provided that without prejudice to any other powers of the Collector, he shall, for the purpose of recovering the said amount, have all the powers which, under the Code of Civil Procedure, 1908, a Civil Court has for the purpose of recovery of the amount due under a decree.

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CHAPTER IV

REVIEW AND APPEAL

32. (1) Any party aggrieved by the certificate issued by the Board under section 24 may within a period of 15 days from the date of receipt of such certificate make an application to the Board for a review.
- (2) The Board shall consider the application and give its decision within a period of 15 days from the submission of such application which shall be final and binding on the parties concerned.
33. (1) Any party aggrieved by the certificate issued by the Board under section 24 may within a period of 30 days from the date of receipt of such certi-

ficcate file an appeal before the Supreme Court on a point of law, in which case no review shall lie.

- (2) Only written submission shall be received and considered by the Supreme Court.

CHAPTER V

MISCELLANEOUS

Board's decision final

34. (1) Notwithstanding anything to the contrary contained in any law, agreement or instrument or any decree or order of a Court, Tribunal, Officer or other authority or of any submission, settlement or standing order, the proceedings and the decisions of the Board under this Act shall be final and conclusive and binding on the parties concerned and shall not be called in question by any Court or other authority.

- (2) The provisions of this Act and of any rules made thereunder shall have effect notwithstanding anything inconsistent therewith contained in any other law for the time being in force or in the Memorandum or Articles of Association or Byelaws or any law other than this Act or in any decree or order of any Court, Tribunal or authority.

Interpretation

35. For the removal of doubts, it is hereby declared that any reference in this Chapter to promoter, manager or officer, of a sick industrial undertaking shall be construed as including a reference to any past or present promoter, director, manager or officer of the sick industrial undertaking.

Saving in respect of acts done in good faith

36. No suit or other legal proceeding shall lie against the Board or nodal agency or any of their officers or other employees or any other person authorised by the Board or nodal agency, as the case may be, to discharge any functions under this Act for any loss or damage caused or likely to be caused by anything which is done in good faith or intended to be done in pursuance of this Act or any other law or provision having the force of law.

Power to make rules

37. (1) The Central Government may, in consultation with the Board make rules not inconsistent with

this Act to provide for all matters for which provision is necessary or expedient for the purpose of giving effect to the provisions of this Act.

(2) In particular and without prejudice to the generality of the foregoing power, such rules may provide for :-

- (a) the conditions and the procedure subject to which the Board may transact its business under this Act;
- (b) the times and places where the Board may meet;
- (c) the duties and conduct, salaries, allowances and conditions of service of officers and other employees of the Board;
- (d) the form of the Certificates to be issued by the Board;
- (e) the manner in which the viability report is to be prepared;
- (f) the manner in which the non-viability report in terms of sub section (3) of section 11 is to be prepared;
- (g) the fee payable in respect of each proposal;
- (h) the establishment and maintenance of provident or other benefit funds for officers and other employees of the Board;
- (i) the compensation that may be paid to the nodal agency for the assistance rendered by it or by the panel of Chartered Accountants and valuers;
- (j) generally, the efficient conduct of the working of the Board; and
- (k) any other matter which is to be, or may be, prescribed.

(3) Any rule which may be made by the Central Government under this Act shall be laid for a period of three months before each House of Parliament.

38. If any difficulty arises in giving effect to the provisions of this Act, the Central Government may, by order, do anything, not inconsistent with the provisions of this Act, for the purpose of removing the difficulty.

Power to
remove difficulties.

THE FIRST SCHEDULE

(See Section 11)

I, _____ do hereby declare that I will faithfully, truly and to the best of my skill and ability execute and perform the duties required of me as Chairman/Member, Officer or other employee (as the case may be) of the Board for Industrial Revival (Board) and which properly relates to the office or position held by me in or in relation to the Board.

I further declare that I will not communicate or allow to be communicated to any person not legally entitled thereto any information relating to the affairs of the Board or to the affairs of any person having any dealing with the Board nor will I allow any such person to inspect or have access to any books or documents belonging to or in the possession of the Board and relating to the business of the Board or the business of any person having any dealing with the Board.

(Signature)

Signed before me.

THE SECOND SCHEDULE

[See Section 18 (2) (a) (i)]

1. The Central Excise & Salt Act, 1944 (1 of 1944)
2. The Industrial Employment
(Standing Orders) Act, 1946 (20 of 1946)
3. The Industrial Disputes Act, 1947 (14 of 1947)
4. The Minimum Wages Act, 1948 (11 of 1948)
5. Employees State Insurance Act, 1948 (34 of 1948)
6. The Employees Provident Fund
Scheme & Family Pension
Funds Act, 1952 (14 of 1952)
7. The Income Tax Act, 1961 (43 of 1961)
8. The Customs Act, 1962 (52 of 1962)
9. The Payment of Bonus Act, 1965 (21 of 1965)
10. The Payment of Gratuity Act, 1972 (39 of 1972)

APPENDIX — III

Broad issues relating to the terms of reference of the Committee on which views were called for from the various organisations.

(A) — Certain broad issues for discussion with FICCI, ASSOCHAM, AIMO and IMC.

The terms of reference of the Committee are enclosed. There are certain related issues concerning finance and management in the rehabilitation of sick industrial units and the views of these Organisations are solicited on the following specific issues :

- 1) What are, in your opinion, the basic causes of spreading sickness in the large and medium industrial units? What are the specific areas which call for special attention of management, financial institutions and banks to tackle as well as prevent new medium and large scale industrial units that are set up in the country, from becoming sick? In other words, whether in your opinion, it would be desirable to improve their appraisal standards regarding financial and other aspects of a project, monitoring the progress of implementation of a project at more frequent intervals, and how far the management of these units could devise steps to liaise with financial institutions and banks in furnishing detailed information on the progress of implementation, problems and critical areas, etc., so as to initiate timely remedial action to prevent sickness in industrial units. If so, in what manner?
- 2) Similarly, in the case of existing industrial units (medium and large), how would you consider it desirable and feasible to acquaint the banks and financial institutions with the problems (existing as well as imminent) of an industrial unit in a more detailed manner as well as more promptly than what it is at present, so as to prevent sickness in an industrial unit; if so, in what manner?
- 3) What are your suggestions to bring about a smooth changeover, wherever warranted, in the management of industrial units which have become sick for various reasons, essentially because of lack of adequate managerial competence and of inability to provide additional finance, so as to prevent a further deterioration in their financial position as well as working, leading to their ultimate closure?
- 4) In your opinion, what are the views on the criteria presently adopted by banks and financial institutions in determining the viability of a sick unit for revival, and would you consider any modifications therein, keeping especially in view the need to have a reasonable time-frame for any programme of revival and also, the equitable sharing of sacrifices — financial and otherwise — involved in it?

- 5) What are your views on the package of various concessions that are being offered by management, banks/financial institutions for reviving a sick industrial undertaking? Would you like to make any suggestions in this regard from the point of view of speedier revival of sick industrial units and their continued working from the long-term point of view?
- 6) Apart from various concessions that are expected from banks/financial institutions and also labour (ref. Item 2(v) of the terms of reference contained in memorandum dated 14-5-1981) in the revival efforts of sick industrial units, what are the sacrifices — financial and otherwise — in your opinion, that need improvement from the management, including staff and shareholders from the point of view of improving the viability of sick units and their speedier revival?
- 7) Similarly, what are the concessions such as forgoing/reduction of any perquisites, increments, terminal benefits, etc., reduction in emoluments and other benefits, reduction in managerial staff strength, deferment of terminal benefits, etc., and forgoing of interest on unsecured deposits/loans by the promoter group that could be considered by the managerial staff, including the Managing Director and whole-time directors, so as to reduce the financial burden on the company, in the rehabilitation programme of sick industrial undertakings in the transitional period? What concessions could be visualised in the case of sick units, in the operations of purchase and sales, especially in the selling commission paid to their sister concerns, if any and when purchases are made through the companies in their Group? What should be the mechanism of doing this?
- 8) What are, in your opinion, the main legal constraints, especially in respect of restructuring of capital base and liabilities, effecting changes in management, to takeover to improve operational and managerial efficiency, MRTP and FERA and IT Act approvals, etc., in rehabilitation of sick units and what are the suggestions for possible legal remedies?
- 9) In your opinion, what are the methods of securing co-operation from the workers in improving productivity and profitability, thus strengthening the viability of industrial units not only from the point of view of preventing an industrial unit from becoming sick but also from the point of view rehabilitating sick units?
- 10) What are your suggestions in effecting a smooth sale of a sick industrial undertaking or in the alternative, effecting the sale of sizeable shareholding in a sick undertaking, in such a manner as to have a management control, from the point of view of protecting public funds,

interests of shareholders, etc., and also revival of a sick industrial unit, where the existing management could not successfully revive the sick unit?

11) In your opinion, what are the suggestions for effecting expeditious merger of sick units with the healthy ones? Do you suggest any changes in the existing laws? If so, in what manner?

12) What are the difficulties that are being faced by the management of a sick unit in disposing of certain non-essential assets/all the assets of the unit (with a special reference to Land Ceiling Acts) so as to improve their financial position through a speedy sale of these assets and realisation of sale proceeds thereof for meeting various obligations including those to banks and financial institutions? How these difficulties could be overcome?

13) What checks and controls would you suggest for containing the preliminary and pre-operative expenses so as to prevent the industrial units from becoming sick even at the stage of going on stream?

14) Any other suggestions which you consider relevant from the point of view of management, in the rehabilitation of sick units, their continued working and nursing them back to normal health.

APPENDIX — III (Contd.)

(B) — Certain broad issues for discussion with the Trade Unions/Organisations (AITUC, INTUC, OTTU, HMS and BMS)

There is a specific term of reference to the Committee on the concessions from the workers in the rehabilitation of sick industrial undertakings; the term of reference is as under :

"To identify in a general way what are the concessions which should normally be made by the various agencies involved in the revival, including management and workers, and in that context, whether sick units should be burdened with obligations like payment of minimum bonus and implementation of various wage awards, etc., which may be having adverse effects on the rehabilitation programmes."

While soliciting the views of Trade Unions/Organisations on the above term of reference, there are certain related issues concerning labour in the rehabilitation of sick industrial undertakings and their views on the following issues may be obtained.

1) Whether in your opinion, it would be desirable to grant exemption to the sick units, say, for a limited period, from the operation of various

wage awards (existing as well as prospective), so as to improve the financial viability in the long run and also their continued working, if so, in what manner?

2) It is reported that many units become sick and are unable to meet even monthly wage payments, because of cash losses being incurred year after year, for various reasons. In such a situation, whether you would like to consider granting (a) exemption from the obligation of payment of minimum bonus; and (b) reduction in wages, postponement of annual increments/modifications in service conditions, etc., if so, in what manner?

3) In case the viability of the sick unit under rehabilitation is, among others, dependent upon rationalisation of labour force, what are the modalities in bringing about suitable rationalisation in this behalf so as to improve the viability of the sick units? Would you like to suggest a suitable machinery for achieving such a rationalisation programme? In this context, we would like to have your reaction to the following :

- (a) payment of terminal and other benefits,
- (b) whether any long term programme for meeting such payment can be considered, because of inability of the sick units to commit such payment immediately.

4) Do you have any suggestions in regard to automation and streamlining of work methods/norms so as to strengthen the viability of sick industrial undertakings, provided the interests of labour are well protected?

5) Any other issues which you consider relevant from the point of view of labour and management, for rehabilitation of sick units, their continued working and nursing them back to normal health.

APPENDIX — III (Contd.)

(C) — Certain broad issues for discussion with the members of IIM and Indian Banks' Association (IBA).

Certain broad issues framed for discussion at the meeting with the trade unions/organisations like AITUC, HMS (New) and HMS and also with associations of trade and industry like FICCI, ASSOCHAM, AIMO and Indian Merchants' Chamber, together with the records of discussions with them have already been circulated vide D.O. letter No. ICD. 785/Com. 2 dated 17 March 1982 to the members of IIM and IBA; while seeking their views on the various observations made by these associations of trade and industry, and also labour, their views on the following specific issues relating directly to their financial involvement

in sick industrial undertakings, apart from those on the terms of reference of the Committee, may be indicated at the meeting on March 27, 1982 for consideration of the Committee :

1) Considering the growing magnitude of sick units, especially in the medium and large scale sectors, involving a substantial amount of credit and investments both from banks and financial institutions, what are, in your opinion, the various difficulties currently faced by banks/financial institutions in bringing about a change in the management of a sick industrial unit assisted by them, so as to protect their financial interests, as well as social and national interests and also in ensuring that the industrial units operate viably from a long term point of view?

2) What are, in your opinion, the suitable criteria (against the background of the existing criteria* being adopted by the financial intermediaries) for determining the viability of a sick industrial unit for undertaking a 'package' of rehabilitation measures, in a reasonable time-frame? In your view, what could be the reasonable time-frame for rehabilitation of a sick industrial unit, especially from the point of view of (a) financial intermediaries, (b) shareholders, (c) debentureholders, and (d) labour?

3) What are the many constraints encountered by the financial intermediaries in the matter of rehabilitation of a sick unit, both financial and legal, and whether, in your opinion, any remedies could be found to overcome these constraints?

4) What are the suggestions which would facilitate the restructuring of the capital base of a sick industrial undertaking from the point of view of rehabilitation and also sustain normal health (i.e. declaration of dividend, running the enterprise without any sort of concessions from the financial intermediaries as well as Government and others, etc. after obtaining the initial 'package' of concessions for rehabilitation) from a long-term point of view?

5) Whether in your opinion, the various concessions being, at present, extended by the financial intermediaries as a 'package' in rehabilitation of a sick industrial undertaking are adequate; whether any change so

* Concept of viability as agreed to in the Standing Co-ordination Committee (SCC) of RBI :

"Viability of a unit should be assessed on a realistic basis i.e. a unit should be considered to be viable if it was in a position to service its debts, at a reasonable rate of interest which could be concessional but not below the minimum lending rate and in no case below the cost of funds to the bank, within a reasonable period, say, about eight to ten years. For this purpose, a distinction will have to be made between reconstruction and rehabilitation of a unit; the former requiring restructuring of its capital and liabilities would need a separate treatment from social angle and such cases would continue to be considered by the IRCI/Screening Committee".

as to improve its viability faster, thus reducing the time-frame for rehabilitation from the present 8 to 10 year period is called for? If so, in what respects?

6) What are the concessions expected by the financial intermediaries from (a) management and workers (para 2 (v) of the terms of reference of the Committee) and (b) other agencies particularly State and Central Governments, in rehabilitation of a sick industrial undertaking?

7) What could be the stand-by institutional arrangements (other than nationalisation) for purchase of undertakings or shares in companies/owning the undertakings, in the absence of private purchasers or in competition with them, in the case of viable units so as to protect to the maximum extent possible, the institutional funds already involved in the undertakings?

8) What are the factors inhibiting expeditious mergers of sick units with the healthy ones and what are the suggestions for expediting such mergers?

9) What are the suggestions for expediting disposal of certain or all the assets of a sick industrial undertaking (e.g. amendment to the Land Ceiling Acts) so as to expedite the legal process for expediting realisation of dues of the financial intermediaries? In this context, a suggestion was made at a meeting the Hon. Finance Minister had in Bombay with the Chief Executives of financial institutions on April 12, 1980 that the financial institutions should be enabled to sell units free from encumbrances. What are your views in the matter?

10) In terms of the recent guidelines issued by the Government of India (vide their Notification No. 7(23)/81-CUS dated the 6th October 1981) on policy for Sick Industry, Government propose to follow a procedure regarding nationalisation or otherwise in all cases irrespective of the fact whether the report is received from banks/financial institutions or from other sources (vide para 2(v)(b) of the Government Notification, copy enclosed). What are your views in the matter as well as the other guidelines mentioned in the above notification especially in the context of protecting the interests of banks and financial institutions and whether any change in the Government guidelines would be necessary? In this context, a note recorded by State Bank of India, raising certain basic issues is enclosed for information; your views are solicited in the matter, especially on the question of denotification.

11) What are the difficulties, if any, faced by the banks and financial institutions in respect of the sick units taken over by the Government under I (D & R) Act, 1951 and what are the remedial measures that could be suggested by them in this regard?

12) What are your views regarding compensation payable by the Government in the event of take-over/nationalisation of sick industrial undertakings by the Government (against the background of earlier nationalisation of sick textile mills and coal mines)?

13) What are, in your opinion, the suggestions to streamline the existing system of :

- a) technical, financial, commercial and managerial appraisal of a project (pre-sanction stage);
- b) review and follow-up during the implementation stage of a project;
- c) follow-up at the post-implementation stage, so as to prevent sickness in an industrial undertaking?

14) Would you like to suggest any modification in the role of nominee directors of banks and financial institutions (both official and non-official) so as to effectively protect their interest?

15) Is it necessary for the banks which grant a substantial amount of credit for meeting working capital needs, to appoint a nominee director on the Board of an industrial undertaking (along with nominee director(s) appointed by the financial institutions or otherwise) to protect their interests?

16) At present, the nominee directors of banks do not enjoy any immunity as available in the case of IDBI, IFCI, etc. Whether in your opinion, any such immunity is necessary in respect of their nominee directors.

17) There is a feeling that the nominee directors of the financial intermediaries are not in a position to play an effective role for various reasons, in rectifying the deficiencies in the affairs of a company (management, financial, technical, marketing, etc.). What are your suggestions to improve this position?

18) Do you suggest the creation of a management pool (financial, technical and marketing) to draw managerial talents in various cadres, so as to fill up the vacuum, if any, when the management of a sick industrial undertaking, is taken over by the financial intermediaries, Government or otherwise? If so, what are the suggestions in this regard?

19) Do you suggest any change in the role of statutory auditors of the companies so as to make them more responsible in discharge of their functions?

20) Whether, in your opinion, any concurrent auditor, auditor or consultant might be appointed by the financial intermediaries so as to effectively monitor the financial, purchase and marketing operations of industrial undertakings under rehabilitation so as to protect their interests and report to them their state of health and progress made from time to time and whether any responsibilities could be cast on them?

21) It is stated that in the U.K., banks obtain what is called a 'Debenture Loan Document' which vests wide powers in banks. The document provides for a comprehensive charge on the fixed and floating assets and at any time after the bank has recalled the advances, the bank has powers to appoint its own Receiver without recourse to a Court of Law. The Receiver so appointed is vested with powers to take possession of all the assets, sell or otherwise deal with such assets, make compromise arrangements, appoint managers to run the undertaking and generally act as the borrowing company's attorney. What are your suggestions for adopting a similar system in our country with suitable modifications, if necessary, in the existing legislations?

22) The Committee has drafted the following definition of a sick industrial undertaking :

"A unit which incurs cash loss for at least the previous accounting year and in the judgement of the bank(s) and/or financial institution(s), is likely to continue to incur cash loss in the current accounting year, and also has an imbalance in its financial structure, such as a current ratio of less than 1:1 and erosion to the extent of 50% or more of net-worth".

Notes

- i) Depreciation on the fixed assets of the company should be charged on the lines indicated in the Companies Act, 1956;
- ii) No revaluation of fixed assets of the company should be taken into account;
- iii) Concepts of 'cash loss', 'current ratio' and 'net-worth' will be defined/explained by the Committee in its main report, so as to avoid ambiguity. (The realisable value of current assets will be taken into account while working out the current ratio of an undertaking).

Provisos

There would be provisos exempting the following categories of units from the contemplated provisions of a Special Legislation for any drastic remedy, although these units would qualify the definition of a sick industrial undertaking.

i) Industrial units affected by external factors such as recession, general strike, severe power cut, etc. peculiar to an industry (say, cotton textiles, jute, sugar, engineering, etc.).

ii) Nascent units experiencing teething troubles, thus requiring a longer period of gestation. What are your views on this definition?

23) What are the ways and means to identify sickness in an industrial undertaking in the initial stage itself and how soon they could be shared with the other financial intermediaries involved in financing the unit, so as to initiate early remedial steps and avoid ultimate sickness?

24) What are the suggestions for improving the existing co-ordination between banks and financial institutions in sharing the details concerning the operations of a company at every stage (appraisal, implementation and post-implementation) and also the security — present and future?

25) What are your suggestions for expediting the legal documentation and other legal formalities, while agreeing to the 'package' of reliefs among the financial intermediaries so to speed up its implementation without any delay, in the interest of the company as well as the financial intermediaries?

26) There is a feeling that the 'package' of concessions is not offered to the sick industrial undertaking in right quantity (at one stage) and at the right time. What are the suggestions to effect improvement in the existing practice?

27) The convertibility clause being stipulated by the financial institutions could be made applicable only when the shareholdings of public financial institutions and Government do not exceed 40% of the total shareholding in a company. What are the specific reasons in restricting this limit to 40%? Will it be possible to take suitable remedial measures to protect the interests of financial institutions, banks and also the public at large only with 40% shareholdings in the event of any necessity, such as revamping of management? What are your views to increase this percentage to over 50% so as to enable the financial intermediaries to acquire controlling interests and take necessary remedial measures to remedy sickness in an industrial undertaking, in particular and other industrial units in general, so as to prevent sickness?

28) In terms of Section 19 of the Banking Regulation Act, no banking company can hold shares in any company as pledgee, mortgagee or absolute owner of an amount exceeding 30% of the paid-up share capital of that company or 30% of the banking company's own paid-up share capital and reserves, whichever is less. In your view, is it necessary

to increase this ceiling so as to enable the banks to convert a portion/all of the overdue interests, and/or principal amount of the loan/cash credit, into the shares of sick industrial undertakings to the extent needed, not only from the point of view of reducing the interest burden as well as repayment obligations, but also from the point of view of acquiring sufficient voting power to effect suitable changes in the management of the company wherever warranted?

29) In terms of RBI instructions contained in their circular No. DBOD. Nat. 2002/C. 473-70 dated 29th July 1970, it has been suggested that in general, guarantees should be obtained only in circumstances absolutely warranted after a careful examination of the circumstances of each case and not as a matter of course. (An important reason for taking guarantees so far has been the feeling that with the signing of the guarantees, the personal interest of the directors and other managerial personnel in the company is strengthened and hence, that the banks taking such guarantees can be reasonably confident of the continuity of good management).

Whether, in your opinion any change in these instructions is necessary, in the context of the growing magnitude of sickness in industrial undertakings and also of enforcing some discipline on the part of the promoters of these companies?

30) Considering the growing magnitude of sickness in industrial undertakings, whether, in your opinion, it is necessary to regard any act of misfeasance or commission and omission, on the part of the management, as economic offence so as to impose deterrent punishment, from the point of view of protecting the interests of the financial intermediaries (their public funds), labourers, etc., and the large productive assets created out of these funds?

31) What is your assessment of the services rendered by various management consultants, particularly in rehabilitation of sick industrial units? How far their services and their forecasts have been found to be useful and desirable in rehabilitation of sick industrial undertakings? Do you suggest any changes in the modus operandi of these consultants, their appointment and fixation of responsibilities?

32) Whether in your view any change is necessary in the existing soft loan schemes being operated by the financial institution? If so, in what respects?

33) Whether in your opinion, is it necessary that before the letters of intent are converted into industrial licences, the views of the financial institutions and banks likely to be involved in meeting the finan-

cial requirements, should invariably be obtained by the Central Government?

34) Supposing it is revealed that a sick industrial undertaking is not likely to be viable from the long-term point of view (after taking into account the cost of various concessions, additional finance involved, etc.), what is the course of action, do you suggest in such cases, having regard to the interests of the financial intermediaries, labourers, shareholders and others?



APPENDIX — IV

Notes prepared by Shri Y. H. Malegam on (A) Modernisation vis-a-vis Tax Concessions and Legislation and (B) Methodology for determining the Reserve Price for the sale of an industrial undertaking.

(A) Note on Modernisation vis-a-vis Tax Concessions and Legislation

1. The Income-tax Act makes provision for the replacement of assets through an allowable deduction for depreciation. The depreciation is calculated at different rates prescribed for different categories of assets which rates are applied on the written down value. When an asset is used for more than one shift, extra shift depreciation is provided, at the rate of 50% of the normal for the second shift and a further 50% of the normal for the third shift. In respect of plant and machinery installed after 31st March 1980 and before 1st April, 1985, an extra depreciation equal at 50% of the normal depreciation is provided in the year of installation. The aggregate amount of depreciation allowed in respect of an asset is however restricted to 100% of its cost.

2. There are no conditions attached to the grant of depreciation, either that it must be provided in the accounts or that it must be separately invested. Depreciation therefore is a non-cash expense for which the assessee gets tax relief. The Companies Act 1956, provides that a Company cannot distribute a dividend without providing for depreciation. However, the Act allows depreciation to be provided in two alternative forms as under :-

(a) On the written down value at rates prescribed under the Income Tax Act or

(b) On the straight-line method at rates which are so derived from the income-tax rates as to ensure that 95% of the cost is written off in the same number of years as would be required to write-off 95% of the cost under the written down method.

3. When a company provides for depreciation under the written down value method, the depreciation as per the accounts will be roughly equal to the depreciation allowed for income tax. However, where a company follows the straight-line method, the depreciation provided in the first few years after the acquisition of the asset will be considerably lower than the depreciation allowed for income-tax. For example, if an asset costs Rs. 10,00,000 and is entitled to depreciation @ 15% and is worked for three shifts, the depreciation provided in the accounts will be Rs. 1,00,000 whereas the depreciation allowed for income tax will be Rs. 3,75,000.

4. If depreciation is allowed for tax purposes to ensure that adequate funds are available for replacement of assets, then it is necessary to ensure that the depreciation so allowed is not distributed as dividend. When the company follows the straight-line method of depreciation, such a danger exists because the disposable profit as per the accounts is higher than the taxable profit (to the extent of difference between the income-tax depreciation and the accounts depreciation) and there is no restriction to the payment of dividends out of this difference.

5. One solution to the above difficulty would be to provide that depreciation allowed for tax purposes should be restricted to the depreciation provided in the accounts. This may create some hardship for highly capital-intensive industries which have a long gestation period since this would postpone the payment of dividend to an abnormally long date and thus make investment in such industries unattractive. The other solution would be, to provide under the Companies Act, that no dividend can be paid unless there is a transfer made from the disposable profits to a Deferred Taxation Reserve to ensure that the Reserve is equivalent to the tax saving arising from the aggregate difference between the depreciation allowed for tax purposes and the depreciation provided in the accounts. In many countries, such a requirement already exists in the Accounting Standards issued by the professional bodies in those countries.

6. The tax laws also provide for the grant of an investment allowance equivalent to 25% of the cost of plant and machinery acquired after 31st March 1978, except for certain cases where the allowance cannot be claimed. The grant of the allowance is subject to certain conditions, namely :-

(a) A reserve equivalent to 75% of the allowance has to be created in the year in which the allowance is claimed and

(b) The reserve has to be utilised within 10 years for acquiring new machinery or plant.

7. The aggregate allowance (both depreciation and investment allowance) available under the tax laws therefore amounts to 125% of the cost of the asset. The cost of replacement of the asset however is normally much more, mainly because of the incidence of inflation. For example, between 1971 and 1979, when the consumer price index showed an annual average increase of 9%, the prices of plant and machinery showed an annual average increase of 15%. Therefore the cost of replacement of an asset having a life of 10 years would have been 404.56% of the original cost.

8. The annexure gives the working to show what would be the result in a hypothetical situation if a company invests the full depreciation and investment allowance outside the business and earns 10% (free of tax) on such investment. It will be seen that even on that basis, the aggregate funds available at the end of the 10 year period would only be 284.149% of the cost leaving a shortfall of 120.41%.

9. If therefore, tax laws have to ensure that companies retain sufficient profits to replace the plant and equipment at the end of its useful life, the following amendments are necessary :-

(a) The Government should publish each year as part of the Finance Act, an index factor which reflects the excess of (i) the general rate of inflation applicable to plant and equipment over (ii) the rate of interest which can be earned on specified investments. For example if the rate of inflation is 15% and the rate of interest is 10%, the index would be 5%.

(b) The assessee should be entitled to claim an additional depreciation calculated by multiplying the allowable depreciation for the year by the index provided that :-

(i) the additional depreciation is provided in the accounts.

(ii) the amount of such additional depreciation is invested in specified investments and used only for replacement of plant.

(c) The interest earned on the specified investments should be free of tax.

10. The Companies Act should also be amended to provide for the creation of a Deferred Tax Reserve.

11. If the above amendments are made, there will be adequate assurance that :-

(a) Temporary tax gains arising from different methods for depreciation used for accounting and tax purposes are not dissipated,

(b) Adequate amounts are charged against the profits to retain amounts necessary for replacement of assets.

(c) The extra depreciation allowed for increases in the cost of replacement is (i) charged in the accounts (ii) separately invested and

(iii) provides adequate financial resources for replacement.

Year		Accumulated Depreciation	Investment Allowance
	Cost	100.00	
1.	Depreciation	37.50	
	I. A.	25.00	25.00
		62.50	25.00
2.	Interest @ 10%	3.75	2.50
	Depreciation	18.75	
		43.75	27.50
3.	Interest	6.00	2.75
	Depreciation	13.125	
		30.625	30.25
4.	Interest	7.913	3.03
	Depreciation	9.188	
		21.437	33.28
5.	Interest	9.623	3.33
	Depreciation	6.431	
		15.006	36.61
6.	Interest	11.228	3.66
	Depreciation	4.502	
		10.504	40.27
7.	Interest	12.801	4.03
	Depreciation	3.151	
		7.353	44.30
8.	Interest	14.396	4.43
	Depreciation	2.206	
		5.147	48.73
9.	Interest	16.056	4.87
	Depreciation	1.544	
		3.603	53.60
10.	Interest	17.816	5.36
	Depreciation	1.081	
		2.522	58.96

11. Interest		19.706	5.90
Depreciation	0.757	0.757	
	<u>1.765</u>	<u>217.524</u>	<u>64.86</u>
100 @ 15% for 10 years.			284.149
			404.56

(B) Note on methodology for determining the Reserve Price for the sale of an industrial undertaking.

1. The Reserve Price can be determined either (i) on the basis of a liquidation value or (ii) on the basis of a 'running concern' value.

2. A liquidation value assumes that the assets would be disposed of on an **individual** basis and not necessarily as an integrated unit and that they need not be used for the purposes for which they were created. Similarly, it assumes that they would be acquired by the purchaser free of all encumbrances including the obligation to take over the services of the staff. If any encumbrances are taken over or if there is any restriction to the free use of an asset e.g. restrictions regarding use or disposal of land or machinery, suitable discounts will have to be given. Similarly, if staff is taken over, adjustment would have to be made for (a) liability for accumulated benefits taken over, (b) retrenchment compensation if staff is to be retrenched, or (c) the burden of surplus staff if it cannot be retrenched.

3. In arriving at a 'running concern' value, three major factors to be considered are :-

- (a) are there any assets which are not essential to the 'running concern' concept e.g. (i) surplus land, (ii) investments, (iii) valuable tenancies;
- (b) are there any assets which are not reflected in the books but which could be exploited e.g. (i) industrial licences, (ii) import or indigenous quotas, etc.;
- (c) does the concern make an operating profit before paying interest?

The assets listed in (a) have to be given their full market value and for the assets listed in (b) suitable adjustment will have to be made to the final value.

4. If the concern does make an operating profit before payment of interest, the current assets must be taken at a fair value and the value of the fixed assets derived from their operating profitability.

5. In arriving at a fair value for current assets the following criteria may be followed :-

- (a) Raw Materials can be valued at their current replacement cost.
- (b) Work in Progress can be valued at :-
 - (i) Realisable value of the finished goods which will be produced from the work-in-progress, less
 - (ii) Fair discount for selling charges, holding costs, etc. before sale can be made
 - (iii) Costs to be incurred to convert work-in-progress into finished goods.
- (c) Finished goods can be valued at:-
Realisable value less fair discount for selling charges, holding costs, etc. before sale can be made.
- (d) Debtors, if taken over must be valued after adjustment for doubtful debts.

6. The value of fixed assets can be derived from their operating capability in the following manner :-

- (i) Profit expected = Return on F. Assets.
+ Return on C. Assets
- (ii) Return on F. Assets = Return on Term Borrowings
+ Return on Own Funds
- (iii) Return on C. Assets = Return on Bank Borrowings
+ Return on Own Funds
- (iv) Normal Pattern of Borrowings = 60% of Fixed Assets and
75% of Net Current Assets
- (v) Assumed Rates of Interest = 14% on Term Borrowing and
19% on Bank Borrowings
- (vi) Assumed Return on Own Funds = 15% after tax i.e. 34.38%
before tax (based on rate of 56.375%).

7. As an example, if profits before interest is Rs. 25 laks and net current assets is Rs. 94.82 lakhs, the calculation would be as under :

$$\begin{aligned}
 \text{Profit (P)} &= \text{Return on F. Assets (X)} + \text{Return on C. Assets (Y)} \\
 P &= [0.14 (0.6X) + 0.3438 (0.4X)] + [0.19 (0.75Y) + 0.3438 (0.25Y)] \\
 &= [0.084X + 0.13752X] + [0.1425Y + 0.08595Y] \\
 &= 0.22152X + 0.22845Y \\
 25 &= 0.22152X + [0.22845 \times 94.82] \\
 &= 0.22152X + 21.66163
 \end{aligned}$$

$$\therefore 0.22152X = 25 - 21.66163 \\ = 3.33837$$

$$\therefore X = \frac{3.33837}{0.22152}$$

= Rs. 15.07 lakhs.

8. The above valuation can be proved as under :

Profit		25.00
Interest :		
14% on (60% of 15) 9.00	1.26	
19% on (75% of 94.82) 71.12	13.51	14.77
Profit after interest		10.23
Tax @ 56.375%		5.77
Profit after taxes		4.46

Return @ 15% on [(15 — 9) + (94.82 — 71.12)] 29.70 = 4.46

9. If the profits before interest is negative, an attempt should be made to see if this becomes positive after fresh investment. For example, assume that after investment of Rs. 65 lakhs. in fixed assets and Rs. 100 lakhs in working capital :-

(i) profit before interest is Rs. 50 lakhs.

(ii) profit before interest is Rs. 60 lakhs

$$P = 0.22152X + 0.22845Y \\ = 0.22152X + 0.22845 (94.82 + 100) \\ = 0.22152X + 44.506629 \\ \therefore 0.22152X = P - 44.506629$$

$$(i) 0.22152X = 50 - 44.506629 \\ = 5.493371$$

$$\therefore X = \frac{5.493371}{0.22152} = 24.80$$

Less : Additional Investment 65.00

\therefore Value of Fixed Assets negative

$$\begin{aligned}
 \text{(ii) } 0.22152X &= 60 - 44.506629 \\
 &= 15.493371 \\
 &= 15.493371
 \end{aligned}$$

$$\therefore X = \frac{15.493371}{0.22152} = 69.94$$

Less : Additional Investment 65.00

Value of Fixed Assets 4.94

10. If the calculation results in a negative value as per example (i) in paragraph 9, then the running concern concept cannot be employed and the reserve price can only be on the basis of liquidation value.

